Attachment 5

Legal Authority White Paper

THE COMMISSION HAS LEGAL AUTHORITY TO IMPLEMENT THE JOINT PROPOSED REFORM FRAMEWORK

The Commission has ample legal authority to adopt each of the proposals in the Joint Proposed Reform Framework ("Framework").[1]

I. With respect to intercarrier compensation, the Framework proposes a multi-year transition that will conclude with a uniform default terminating rate of $0.0007 per minute for all traffic routed to or from the PSTN, regardless of provider or technology.[2] The Framework also calls for a cap on originating access and other intercarrier compensation rates. The Commission has multiple, mutually reinforcing sources of legal authority on which it can rely to adopt these proposed reforms, and the Commission may find that it can put its reform efforts on the most solid footing by articulating *each* of these sources of authority.

A. The Commission can rely on its rulemaking authority to implement section 251(b)(5) to adopt a uniform default rate for all traffic routed to or from the PSTN. The Commission has previously stated that the compensation regime in section 251(b)(5) includes the transport and termination of *all* "telecommunications" involving at least one LEC and makes no distinctions based on jurisdiction or type of service. All traffic currently subject to either tariffed access charges or reciprocal compensation charges falls within section 251(b)(5), because it necessarily involves a LEC on at least one end. With respect to that traffic, the Supreme Court has made clear that the Commission "has jurisdiction to design a pricing methodology" to

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[1] This white paper is a joint filing by the parties to the Framework. The signatories may have differing views on certain issues related to intercarrier compensation and universal service reform, and do not intend for this filing to alter their prior advocacy or constrain their future advocacy on these issues. Moreover, individual parties have proposed additional, in some cases complementary, theories in their separate filings that may also provide support for the Framework. This white paper should not be interpreted as a shift in the parties' individual views regarding the scope of and constraints on the Commission's statutory authority.

[2] Carriers would remain free to depart from the default rate through voluntary agreements with other carriers.

implement section 251(b)(5) and the related pricing standards in section 252(d). *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 385 (1999). Using that authority, the Commission may establish a pricing methodology that includes a uniform default rate for all traffic subject to section 251(b)(5). The Commission can also rely on that authority, along with its authority under section 251(g), to cap originating access and other intercarrier compensation rates. At the same time, the Commission can offer carriers a meaningful opportunity to recover additional compensation for the work they perform from their customers and a temporary access revenue replacement mechanism.

B. In addition to section 251(b)(5), the Commission can rely on sections 201 and 332 to assert authority over all traffic on the PSTN, including traffic currently subject to state-law intercarrier compensation regimes. Specifically, the Commission may rely on the "impossibility," or "inseverability," doctrine to extend its authority under sections 201 and 332 to all traffic routed to or from the PSTN — including Voice-over-Internet Protocol ("VoIP") traffic, which the Commission can conclude is all interstate for jurisdictional purposes — by adopting rules that preempt, prospectively, state intercarrier compensation rules that differ from the uniform federal regime, whether with respect to originating or terminating traffic.

Indeed, the Commission can rely on dramatic marketplace and technological changes in recent years to find that *all* traffic routed to or from the PSTN — whether TDM, wireless, or VoIP — is now inseverable. As consumers migrate in ever greater numbers to flat-rated, any-distance plans that include location-independent features — such as number assignment, multi-phone call-answering options, and mobility — the Commission may determine that carriers will find it more and more difficult to identify different types of traffic reliably, let alone to jurisdictionalize the traffic for billing purposes. The Commission may further find that some any-distance, any-phone services are *intended* to transcend legacy geographic and service distinctions, and their providers have no business incentive to invest in the capabilities to align these new services with legacy jurisdictional distinctions. The Commission has applied the inseverability doctrine in numerous cases where, as it may find here, it was not practical, in light of economic and operational considerations, to separate a service into “interstate” and “intrastate” components, even though it might have been *technically* possible to do so.

Moreover, the Commission can find that the continued application of state intercarrier compensation rules that differ from the uniform federal regime would pose a direct obstacle to the accomplishment of federal policy. For more than a decade, the Commission has expressed a goal of adopting a *uniform* intercarrier compensation regime, and it can find that any state regulations that depart from the uniform federal regime would necessarily stand as an obstacle to the Commission’s policy goals. Genuine intercarrier compensation reform cannot succeed for *any* class of traffic — including traffic over which the Commission has undisputed jurisdiction — unless the reforms encompass *every* class of traffic. Otherwise, artificial rate disparities for functionally substitutable services will continue to destabilize the industry as a whole. In addition, the Commission has authority to cap originating access and other intercarrier compensation rates to ensure that those other rates are not used to evade the uniform default rate for terminating traffic. The Commission can find that preemption of state intercarrier compensation regimes that vary from the uniform federal regime is therefore necessary to prevent methodological inconsistencies from thwarting the Commission’s lawful exercise of its authority over interstate communications.

C. The Commission can select $0.0007 per minute as the ultimate, uniform default rate for all traffic, regardless of provider or technology. As a result of prior Commission orders, that is *already* the default rate for a substantial portion of the traffic that carriers exchange today, such as wireless and ISP-bound traffic. A rate of $0.0007 per minute is also consistent with the rates contained in some recently negotiated agreements between ILECs and CLECs. Courts and the Commission have repeatedly recognized that rates negotiated through voluntary, arms-length negotiations are just and reasonable rates.

D. The Commission also has authority to adopt reasonable interim rules to ease the transition to a unified intercarrier compensation regime. Under the Framework, intrastate access, interstate access, and reciprocal compensation rates will be reduced gradually over a period of years to the end-state default rate of $0.0007 per minute. A similar transition will apply to VoIP traffic routed to or from the PSTN, although such traffic initially will be subject either to interstate access or reciprocal compensation rates only. The rates applicable to VoIP traffic, as with all other traffic on the PSTN, will decline and converge over time to $0.0007 per minute.

In a variety of different contexts — including intercarrier compensation — the Commission has found it appropriate to adopt transitional mechanisms that advance its policy goals, while avoiding a "flash cut" to the end state of the new policy regime. Courts have afforded the Commission substantial leeway in crafting transitional mechanisms, especially where — as here — the Commission adopts bright-line transitional rules that strike a careful balance between the efficiency gains of the new policy and the costs of upsetting settled expectations.

E. The Framework proposes two key access recovery opportunities for carriers that may face reduced access revenues as a result of decreases in intercarrier compensation. First, carriers will be permitted — but not required — to increase their subscriber line charges ("SLC") by up to $0.75 per year. The Commission clearly has authority to take this step. Indeed, the

Commission raised the SLC cap in connection with its prior reforms of the interexchange marketplace, and the courts affirmed that decision. The same would be true here, where the increased SLC cap would also be designed to allow carriers to *replace* lost intercarrier compensation revenue. Courts would grant substantial deference to the Commission's determination that the benefits of this policy would far outweigh its costs.

Second, the Framework proposes creation of a temporary "access replacement mechanism" that will provide universal service funding for carriers that face a net loss of intercarrier compensation revenue as a result of the Framework and are unable to recoup that revenue through SLC increases. This mechanism, too, is well within the Commission's discretion. The Commission has taken similar steps in the past, and this access replacement mechanism is consistent with the statutory mandate that universal service support be "explicit." 47 U.S.C. § 254(e). The access replacement mechanism is also well within the Commission's authority, discussed above, to adopt reasonable transitional measures to avoid undue disruption resulting from new policies.

II. The Commission has ample statutory authority to support broadband service with universal service funding. Section 254(b) — which lists the principles upon which the Commission "shall" base its universal service policies — provides that "[a]ccess to *advanced* telecommunications and *information services* should be provided in all regions of the Nation," and that "[c]onsumers in all regions of the Nation, . . . should have access to telecommunications and *information services*, including interexchange services and *advanced* telecommunications and *information services*, that are reasonably comparable to those services provided in urban areas[.]" 47 U.S.C. § 254(b)(2)-(3) (emphases added). Section 706 of the Telecommunications Act of 1996 ("1996 Act") further provides that the Commission "shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans" in areas where broadband is not currently being deployed. *Id.* § 1302(a). The American Recovery and Reinvestment Act of 2009 also mandates that the Commission "shall seek to ensure that all people of the United States have access to broadband capability." *Id.* § 1305(k)(2).

Although certain provisions of section 254 refer to "telecommunications carriers" or "telecommunications services," those provisions are not sensibly read to restrict the Commission's authority to provide universal service support for broadband. Multiple other provisions of section 254 reject a static focus on legacy technologies, defining "universal service" as an "*evolving* level of telecommunications services that the Commission shall establish periodically under this section, *taking into account advances* in telecommunications *and information technologies and services*." *Id.* § 254(c)(1) (emphases added). That interpretation is further reinforced by section 706(b), which provides that if the Commission finds that advanced telecommunications capability is not being deployed to all Americans, it "shall take immediate action to accelerate deployment of such capability" in the areas that lack access to broadband. *Id.* § 1302(b). At a minimum, there is sufficient ambiguity about the scope of section 254 that the Commission's reasonable interpretation of that provision as encompassing broadband service would be entitled to deference from a reviewing court.

III.A. Lastly, the Commission has authority to eliminate outdated service obligations such as those imposed under the Commission's eligible-telecommunications-carrier ("ETC") regulations or other carrier-of-last-resort ("COLR") rules. Going forward, state or federal service obligations must apply only to funded carriers in those areas where they receive explicit support — regardless of those carriers' legacy regulatory status. Current federal ETC obligations, however, require designated carriers to provide supported services throughout their service areas, *regardless* of whether they are receiving high-cost support for those services. Similarly, some states have COLR obligations that require incumbent LECs to provide service in a given area, sometimes at reduced rates. In today's dynamic marketplace, these regulations are not only unnecessary but actually *undermine* Congress's and the Commission's universal service goals by locking consumers into legacy technologies and deterring carriers from deploying broadband and IP-enabled services. Existing ETC and COLR regulations, where they apply, inefficiently skew the market and make it difficult (or even impossible) for carriers to upgrade from legacy architecture, thus diverting capital that could be used for broadband deployment. Those rules — which generally apply only to incumbent LECs — also effectively impose unfunded mandates and are inconsistent with a technologically neutral, procurement-model approach to universal service, in which the Commission would make explicit agreements with providers to serve a specific area that otherwise would not be served for a specific period of time in return for a specific amount of universal service funding.

B. The Commission plainly has authority to reform legacy ETC obligations. When it eliminates the existing high-cost universal service programs, the Commission can simultaneously eliminate any ETC obligations that require carriers to provide legacy services. On a going-forward basis, the Commission also has authority under section 214 to ensure that any mandatory service obligations apply *only* when an ETC actually receives high-cost support for a given geographic area. It is already the case today that carriers receive no federal high-cost funding in some areas, and legacy ETC obligations for those carriers in those areas should be eliminated immediately upon adoption of the Framework.

C. While many states that had COLR obligations have either eliminated or scaled them back, other states have not. The Commission can encourage states to transform their legacy service obligations so that they promote, rather than frustrate, the Commission's universal service goals. For the states that refuse to undertake such reforms or that fail to provide explicit universal service support that fully compensates carriers that have elected to continue satisfying the state's service obligations, the Commission can preempt legacy service obligations as inconsistent with federal policy. The Commission can rely on two, mutually reinforcing sources of authority for such preemption.

First, the Commission can conclude that state legacy service obligations negate the Commission's policy of ensuring that broadband is deployed throughout the nation. The Commission has preempted state law in numerous cases where it was not practical, in light of economic and operational considerations, to separate the "interstate" and "intrastate" components of a service, even though it might have been *technically* possible to do so. Here, it would be impossible to limit the detrimental effect of state service obligations to the intrastate jurisdiction alone, as such regulations also make it infeasible for carriers to deploy jurisdictionally *interstate* broadband facilities in many high-cost areas. Legacy service obligations that compel incumbents to provide service may be unfunded mandates and are flatly inconsistent with a technologically neutral, procurement-model approach to universal service.

Second, the Commission has authority under section 254(f) to preempt state legacy service obligations that are "inconsistent" with the Commission's rules, that "burden" federal universal service mechanisms, or that are not "equitable and nondiscriminatory." 47 U.S.C. § 254(f). State legacy service obligations satisfy each of these criteria for preemption.

I. THE COMMISSION HAS LEGAL AUTHORITY TO ADOPT A MULTI-YEAR TRANSITION THAT CONCLUDES WITH A UNIFIED DEFAULT RATE OF $0.0007 PER MINUTE FOR ALL TRAFFIC ROUTED TO OR FROM THE PSTN

A. The Commission Has Authority Under Section 251(b)(5) To Achieve Comprehensive Intercarrier Compensation Reform

1. Section 201(b) of the Communications Act grants the Commission authority to "prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of this chapter." 47 U.S.C. § 201(b). The Supreme Court has made clear that the Commission's rulemaking authority under section 201(b) is *not* limited to jurisdictionally "interstate" matters, but instead extends to all "'provisions of th[e] [1996] Act,' which include §§ 251 and 252, added by the Telecommunications Act of 1996." *Iowa Utils. Bd.*, 525 U.S. at 378. Under that authority, the Commission may promulgate rules adopting a uniform default rate for all traffic routed to or from the PSTN — regardless of provider or technology — that falls within the scope of section 251(b)(5).[3]

Section 251(b)(5) imposes on "local exchange carrier[s]" the "duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications." 47 U.S.C. § 251(b)(5). The Commission has previously concluded that this provision extends to the transport and termination of *all* "telecommunications" involving at least one LEC, and it makes no distinctions based on jurisdiction ("local," "toll," "interstate," or "intrastate") or type of service ("exchange access," "information access," or "exchange service"). Congress also made clear in section 251(g) that the Commission has authority to "explicitly supersede[]" existing rules governing exchange access and other intercarrier arrangements, including those governing "receipt of compensation." *Id.* § 251(g).

[3] Under the Framework, the uniform default rate would apply *only* to traffic that is routed to or from an end user on the PSTN. IP-to-IP traffic would be unregulated.

In the *ISP Remand Order*, the Commission stated that section 251(b)(5) is not limited to "local" traffic, but instead extends to "the transport and termination of *all* telecommunications exchanged with LECs." *ISP Remand Order*[4] ¶¶ 15-16, 34, 45 (emphasis added). The Commission has reiterated that holding several times, and its most recent order relying on this theory was upheld by the D.C. Circuit. *See Core Communications, Inc. v. FCC*, 592 F.3d 139, 143-46 (D.C. Cir.), *cert. denied*, 131 S. Ct. 597, 626 (2010).[5] Moreover, the Commission has elected to treat intraMTA wireless traffic as part of the section 251(b)(5) regime. *See Local Competition Order*[6] ¶¶ 1036, 1041 (bringing LEC-wireless intraMTA traffic within the section 251 framework).[7]

Furthermore, as the Commission has interpreted it, section 251(b)(5) applies not only to the exchange of traffic between two LECs (or between a LEC and a CMRS carrier), but also to the terms on which LECs receive terminating traffic from non-LECs, such as IXCs. The Commission has concluded that section 251(b)(5) extends to the exchange of *any* traffic involving a LEC at one end. *See 2011 NPRM* ¶ 513; *2008 NPRM* ¶ 10; *ISP Remand Order* ¶¶ 26, 31-32. Though the *obligation* to establish reciprocal compensation arrangements for the

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[4] Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, *Intercarrier Compensation for ISP-Bound Traffic*, 16 FCC Rcd 9151 (2001).

[5] *See also, e.g.*, Order on Remand and Further Notice of Proposed Rulemaking, *Intercarrier Compensation for ISP-Bound Traffic*, 24 FCC Rcd 6475, ¶ 15 (2008) ("*2008 NPRM*") (noting that section 251(b)(5) is broad enough to cover "the transport and termination of all telecommunications exchanged with LECs"); Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, *Developing an Unified Intercarrier Compensation Regime*, 26 FCC Rcd 4554, ¶¶ 512-515 (2011) ("*2011 NPRM*").

[6] First Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 FCC Rcd 15499 (1996) ("*Local Competition Order*").

[7] As discussed further below in Section I.A.3, the Commission has authority under sections 201 and 332 over all intercarrier compensation charges imposed by wireless providers.

transport and termination of telecommunications falls on LECs, the Commission has concluded that Congress did not limit the class of potential *beneficiaries* of that obligation to other LECs.

The Commission can further conclude that the statutory structure as a whole belies the argument that Congress meant to deprive the Commission of authority to address intercarrier compensation issues for traffic that is deemed to be neither "local" (and undisputedly covered by section 251(b)(5)) nor "interstate" (and undisputedly covered by section 201(a)). Efforts to carve up the Commission's rulemaking authority on the basis of such legacy jurisdictional categories are strikingly similar to the unavailing attacks in the 1990s on the Commission's jurisdiction to implement sections 251 and 252 more generally. Here, as in that context, the attempt to "produce[] a most chopped-up statute" along jurisdictional lines is flawed both because it violates the statutory text and because it is "most unlikely that Congress created such a strange hodgepodge." *Iowa Utils. Bd.*, 525 U.S. at 381 n.8. Indeed, it would have made no sense for Congress to have authorized the Commission to reform intercarrier compensation rules relating to "local" and "interstate" traffic but not the rules applicable to the one class of traffic — intrastate toll traffic — that is subject to the *highest* charges.

In sum, section 251(b)(5), as interpreted by the Commission, is broad enough to capture *all* traffic currently subject to the existing, disparate intercarrier compensation regimes, including the reciprocal compensation regime and the interstate and intrastate access regimes.

2. The Commission can find that section 251(g) provides additional support for this interpretation of section 251(b)(5). That provision *temporarily* grandfathers the pre-1996 Act rules — including rules regarding "receipt of compensation" — governing "exchange access, information access, and exchange services," until the Commission chooses to "explicitly supersede[]" those rules "by regulation[]." 47 U.S.C. § 251(g); *see 2008 NPRM* ¶ 16. The

Commission can conclude that there would have been no need for Congress to have preserved those legacy rules against the effects of section 251 if section 251(b)(5) did not in fact address the "receipt of compensation" for the traffic covered by that section.

Nothing in the Commission's precedent precludes this interpretation of section 251(b)(5). Granted, in the *ISP Remand Order*, the Commission noted that services falling within the scope of section 251(g) "remain subject to Commission jurisdiction under section 201 (or, to the extent they are *intra*state services, they remain subject to the jurisdiction of state commissions)." *ISP Remand Order* ¶ 39. But this does not foreclose the Commission from exercising jurisdiction over intrastate access charges. There is no question that section 251(g) temporarily preserves the regulatory status quo for all traffic within that provision's scope until explicitly superseded by the Commission, "includ[ing] intrastate access services."[8] Indeed, "although section 251(g) does not directly refer to intrastate access charge mechanisms, it would be incongruous to conclude that Congress was concerned about the effects of potential disruption to the interstate access charge system, but had no such concerns about the effects on analogous intrastate mechanisms." *Local Competition Order* ¶ 732. The only dispute is whether, as the Commission has proposed, it can "supersede that carve-out" by "replac[ing] intrastate access regulation with some alternative mechanism" of the Commission's design as part of a comprehensive approach to intercarrier compensation. *2005 FNPRM* ¶ 79.

The only logical answer is yes. The sole reason that the "section 251(g) carve-out includes intrastate access services," *id.*, is that, if it did *not* include them, section 251(b)(5) could have operated to eliminate those access charges immediately. Once the Commission removes

[8] Further Notice of Proposed Rulemaking, *Developing a Unified Intercarrier Compensation Regime*, 20 FCC Rcd 4685, ¶ 79 (2005) ("*2005 FNPRM*"); *see also 2011 NPRM* ¶ 514; *ISP Remand Order* ¶ 39.

this or any class of traffic from the scope of section 251(g) by superseding previous rules, that traffic becomes subject to section 251(b)(5) — as it would have been from the beginning if Congress had not temporarily grandfathered such traffic from the effects of section 251 when it enacted the 1996 Act. And because the Commission has plenary authority under *Iowa Utilities Board* to implement section 251(b)(5), it has authority to address compensation issues involving intrastate access traffic.

Section 251(g), moreover, allows the Commission to cap originating access and other intercarrier compensation rates in connection with the Framework. As the Commission has explained, although section 251(b)(5) refers only to the "transport and termination" of telecommunications, the statute does not "preclude[] [the Commission] from moving originating access charges to a new methodology." *2011 NPRM* ¶ 517. And section 251(g) expressly authorizes "'regulations prescribed by the Commission' to replace the current access charge system," which may address "originating access charges," as well as terminating charges. *Id.*

3. Nothing in section 252 of the 1996 Act limits the Commission's section 201(b) authority to promulgate intercarrier compensation rules that establish a uniform default rate for all traffic covered by section 251(b)(5).

Section 252 gives state commissions authority over the negotiation and arbitration of interconnection agreements. And section 252(c)(2) authorizes states to set rates in the course of interconnection agreement arbitrations "according to subsection (d) of this section." 47 U.S.C. § 252(c)(2). But a significant amount of traffic that is covered by section 251(b)(5) is entirely outside the authority that section 252 confers on state commissions. That is so because section 252(d)(2) authorizes state commissions to review only the reciprocal compensation rates that *incumbent* LECs charge. *See id.* § 252(d)(2)(A) ("For the purposes of compliance *by an* *incumbent local exchange carrier* with section 251(b)(5) . . . .") (emphasis added). As a result, that provision does not by its terms encompass either any traffic exchanged without involvement of an incumbent LEC or any rates that non-incumbent LECs charge, even if an incumbent LEC is involved.[9] The Commission can set a uniform default rate for all of this traffic simply by exercising its section 201(b) rulemaking authority to establish rules implementing section 251(b)(5).

For traffic that is exchanged with incumbent LECs, the Commission has *independent* authority under section 201(b) over jurisdictionally interstate traffic. Congress has explicitly given the Commission authority to ensure that rates for "interstate" communications services are "just and reasonable." *Id.* § 201. The D.C. Circuit recently upheld the Commission's authority under section 201 to enact compensation rules regarding interstate traffic, regardless of whether that traffic is also encompassed within section 251(b)(5). *See Core*, 592 F.3d at 143-46.[10] This authority will include authority over all VoIP traffic, upon a Commission finding that all such traffic is inseverable and, therefore, interstate for jurisdictional purposes. Although the parties to the Framework have differing views about whether all VoIP traffic is currently interstate for jurisdictional purposes, all agree that the Commission can make that finding on a prospective basis.

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[9] Where no incumbent LEC is involved, the section 252 regime for the creation of interconnection agreements — and state authority as part of that regime — does not apply at all. *See* 47 U.S.C. § 252(a)(1) (providing that "an incumbent local exchange carrier may negotiate and enter into a binding agreement" with a requesting carrier "without regard to the standards set forth in" section 251(b) and (c)); *id.* § 252(b)(1) (state commissions may "arbitrate any open issues" during the period from 135 to 160 days after "an incumbent local exchange carrier receives a request for negotiation under this section").

[10] *See also* Order, *Access Charge Reform*, 12 FCC Rcd 10175, ¶ 7 (1997) (noting that "no one has questioned (or plausibly could question)" that section 201(b) provides the Commission with "authority over interstate access charges"); *2011 NPRM* ¶ 510 (noting that "reducing interstate access charges falls well within our general authority to regulate interstate access under sections 201 and 251(g)").

The Commission also has independent authority over intercarrier compensation charges imposed by wireless carriers. *See* 47 U.S.C. § 332(c).[11] Indeed, because Congress has expressly preempted state "regulat[ion] [of] . . . the rates charged by any commercial mobile service," the Commission can assert *exclusive* authority to regulate all intercarrier compensation charges imposed by wireless providers. *Iowa Utls. Bd. v. FCC*, 120 F.3d 753, 800 n.21 (8th Cir. 1997) (subsequent history omitted).

As to the remaining traffic exchanged with incumbent LECs, nothing in section 252(d)(2)(A) limits the Commission's authority to promulgate rules establishing a uniform default rate for this traffic. Section 252(d)(2) provides that, in determining whether an incumbent LEC has complied with section 251(b)(5), "a State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable" unless those terms "provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination" of telecommunications traffic and are a "reasonable approximation of the additional costs of terminating such calls." 47 U.S.C. § 252(d)(2)(A). As the Supreme Court has explained, "[n]one of the statutory provisions" in section 252 regarding state commission review of interconnection agreements "displaces the Commission's general rulemaking authority" or "preclude[s] the Commission's issuance of rules to guide the state-commission judgments." *Iowa Utils. Bd.*, 525 U.S. at 385. Indeed, the Court expressly held that "the

[11] *See also* Declaratory Ruling, *Petitions of Sprint PCS and AT&T Corp. for Declaratory Ruling Regarding CMRS Access Charges*, 17 FCC Rcd 13192, ¶¶ 8-12 (2002); Second Report and Order, *Implementation of Sections 3(n) and 332 of the Communications Act*, 9 FCC Rcd 1411, ¶ 179 (1994).

Commission has jurisdiction to design a pricing methodology" to implement the pricing standards in section 252(d). *Id.*[12]

The Eighth Circuit has endorsed a relatively narrow interpretation of the Supreme Court's decision in *Iowa Utilities Board*, concluding that the Commission's role is limited to resolving " 'general methodological issues' " and that "[s]etting specific prices goes beyond the [Commission's] authority to design a pricing methodology." *Iowa Utils. Bd. v. FCC*, 219 F.3d 744, 757 (8th Cir. 2000) (citation omitted), *aff'd in part*, *rev'd, in part*, 535 U.S. 467 (2002). But nothing in the Supreme Court's decision suggests that "design[ing] a pricing methodology" is at the *outer limit* of the Commission's authority; that decision is equally open to the interpretation that adopting a pricing methodology, such as the TELRIC rules, is comfortably within the Commission's authority under section 201(b) to adopt rules to implement section 252(d)(2), rather than at the outer limits of that authority. *See* 525 U.S. at 385 (finding that "the Commission has jurisdiction to design a pricing methodology").

In any event, even if the Commission were limited to adopting a "pricing methodology" — and nothing in the Supreme Court's *Iowa Utilities Board* decision suggests that this is the case — it could adopt a "methodology" that caps reciprocal compensation rates at the uniform

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[12] The Commission has previously exercised this authority to design a pricing methodology to implement the standards in section 252(d). In the *Local Competition Order*, the Commission held that "states that elect to set rates through a cost study *must* use the forward-looking economic cost-based methodology" known as "TELRIC." *Local Competition Order* ¶¶ 1054-1058. In adopting the Framework, the Commission would need to revisit (and reverse) that determination. Nothing in the statute compelled the Commission to adopt the TELRIC methodology for § 252(d)(2). And the Commission could justify its departure from its initial interpretation of this section with the following explanation: Not only is the TELRIC methodology incompatible with the clearly demonstrated need for a uniform intercarrier compensation regime, but also the Commission has moved away from TELRIC pricing for most traffic subject to § 251(b)(5), through its adoption of the mirroring rule. *See FCC v. Fox Television Stations, Inc.*, 129 S. Ct. 1800, 1811 (2009) (holding that an agency may change its interpretation of a statute if it "display[s] awareness that it *is* changing position," and "show[s] that there are good reasons for the new policy").

federal default rate in the absence of a voluntary agreement, and instructs carriers to recover, through a temporary access recovery mechanism and from their customers, any additional compensation for the work they perform. Indeed, the statute expressly provides that "arrangements that afford the mutual recovery of costs" for purposes of section 252(d)(2) include "bill-and-keep arrangements," 47 U.S.C. § 252(d)(2)(B)(i), under which "each carrier recovers its costs from its own end-users" rather than from the other carrier, *WorldCom, Inc. v. FCC*, 288 F.3d 429, 431 (D.C. Cir. 2002). Because an arrangement in which a carrier recovers *all* of its costs from its customers and *none* from other carriers could satisfy section 252(d)(2), it follows that section 252(d)(2) can be satisfied through an arrangement where a carrier recovers *some* costs from the originating carriers and some from its customers and other methods.

Lastly, even for the traffic to which it applies, section 252(d)(2)(A) establishes limits only on "[s]tate commission" review of the reciprocal compensation provisions of interconnection agreements, *id.* § 252(d)(2)(A), without purporting to limit the *Commission's* authority over reciprocal compensation rates. In contrast, the following subsection prohibits certain types of rate-regulation proceedings and applies to both "the Commission [and] any State commission," *id.* § 252(d)(2)(B)(ii). Therefore, as the Commission argued to the D.C. Circuit, the Commission could conclude that section 252(d)(2)(A) does not constrain *its* rulemaking authority even with respect to rates incumbent LECs charge for jurisdictionally intrastate traffic.[13]

[13] Br. of FCC at 33-34, *Core Communications, Inc. v. FCC*, Nos. 08-1365, 09-1046, 08-1393, 09-1044 (D.C. Cir. filed June 19, 2009).

B. The Commission Has Authority To Find That All Traffic Is Now "Inseverable" and To Preempt State Intercarrier Compensation Regimes That Differ from the Uniform Federal Regime Because They Undermine Important Federal Policies

As explained above, the Commission can establish a uniform default rate for all traffic by promulgating rules implementing the reciprocal compensation obligation in section 251(b)(5) and the related pricing standards in section 252(d)(2). The Commission also has authority to establish a uniform default rate for all traffic, regardless of provider or technology, pursuant to its authority under sections 201 and 332 and the "inseverability" doctrine. As explained above, even without that doctrine, the Commission has authority under those provisions to establish a uniform default rate for jurisdictionally interstate traffic — which includes all VoIP traffic upon a Commission finding that all such traffic is inseverable and, therefore, interstate for jurisdictional purposes — and intercarrier compensation charges imposed by wireless carriers. *See supra* Section I.A.3. The Commission can use that authority to extend the uniform default rate to jurisdictionally intrastate traffic by relying on dramatic marketplace and technological changes in recent years to find that *all* traffic routed to or from the PSTN is now inseverable as a practical matter. The Commission may also use that authority to cap originating access and other intercarrier compensation rates. Any state intercarrier compensation rules that differ from the uniform federal regime would necessarily conflict with federal policy and pose a direct obstacle to the Commission's longstanding goals of eliminating inefficient arbitrage opportunities and promoting broadband deployment. The Commission's authority under sections 201 and 332 reinforces its authority under section 251(b)(5) to establish a pricing regime that includes a uniform, default rate for all traffic routed to or from the PSTN.

1. The Commission Has Authority under the Communications Act To Regulate Intrastate Services When They Are Inseverable from Interstate Services and the Application of State Law Would Interfere with the Commission's Policy Objectives

Although section 2(b) of the Communications Act, 47 U.S.C. § 152(b), generally prohibits the Commission from exercising "jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications," it is well established that the "inseverability" or "impossibility" doctrine authorizes the Commission to regulate nominally "intrastate" traffic or services when it is "impossible or impractical to separate the service's intrastate from interstate components and the state regulation of the intrastate component interferes with valid federal rules or policies." *Vonage Order*[14] ¶ 17 (citing *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 376 n.4 (1986)); *see also Public Serv. Comm'n of Md. v. FCC*, 909 F.2d 1510, 1514-15 (D.C. Cir. 1990).[15]

The standard for applying the inseverability doctrine is not whether it is *technically* impossible to single out intrastate communications. *See Vonage Order* ¶¶ 23, 29, 37. The dispositive question, instead, is whether, in light of "practical and economic considerations," interstate traffic can be separated from intrastate traffic and afforded differential treatment. *California v. FCC*, 39 F.3d 919, 932-33 (9th Cir. 1994). That focus on economic and practical considerations reflects the longstanding rule that carriers are not required to expend resources or modify their services "merely to provide state commissions with an intrastate communication

[14] Memorandum Opinion and Order, *Vonage Holdings Corp. Petition for Declaratory Ruling Concerning an Order of the Minn. Pub. Utils. Comm'n*, 19 FCC Rcd 22404 (2004).

[15] In *Louisiana PSC*, the Court held that it was feasible, as an accounting matter, for the federal government and the states to prescribe different depreciation rates for the same equipment. *See* 476 U.S. at 358-59, 375-76. As explained below, however, the criteria for application of the inseverability doctrine are plainly met here.

they can then regulate." *Minnesota Pub. Utils. Comm'n v. FCC*, 483 F.3d 570, 578 (8th Cir. 2007).[16]

The Commission has applied the inseverability doctrine in numerous cases where it was not practical, in light of economic and operational considerations, to separate the interstate and intrastate services, even though it might have been *technically* possible to do so. For example, the Ninth Circuit upheld the Commission's finding in the *Computer Inquiry* orders that jurisdictionally mixed information services were inseverably interstate, based on the Commission's determination "that it would not be economically feasible for the BOCs to offer the interstate portion of such services on an integrated basis while maintaining separate facilities and personnel for the intrastate portion." *California*, 39 F.3d at 932. Even if it were technically "possible to comply with both the states' and the [Commission]'s regulations," the court deferred to the Commission's finding that it was "highly unlikely, due to practical and economic considerations," that such a jurisdictional division would succeed. *Id.* at 933. The Fourth Circuit similarly upheld the Commission's decision applying the inseverability doctrine to consumer premises equipment on the ground that it was "not feasible, *as a matter of economics and practicality of operation*," to have separate state and federal regulation of the CPE, despite the fact that the CPE in question was used 97 to 98 percent of the time for "intrastate" calls.[17]

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[16] *See also Vonage Order* ¶ 25 (holding that "to require Vonage to attempt to incorporate geographic 'end-point' identification capabilities into its service solely to facilitate the use of an end-to-end approach would serve no legitimate policy purpose" and would unreasonably "mold[] this new service into the same old familiar shape").

[17] *North Carolina Utils. Comm'n v. FCC*, 537 F.2d 787, 791 (4th Cir. 1976) ("*NCUC I*") (emphasis added); *see id.* at 796 (Widener, J., dissenting); *North Carolina Utils. Comm'n v. FCC*, 552 F.2d 1036, 1044, 1046 (4th Cir. 1977) ("*NCUC II*").

2. *The Commission Has Authority To Find That Dramatic Technological and Marketplace Changes Have Rendered All Traffic Inseverable as a Practical Matter*

As explained above, the Commission has authority over jurisdictionally interstate traffic and the intercarrier compensation charges imposed by wireless carriers. *See* 47 U.S.C. §§ 201, 332(c); *2011 NPRM* ¶¶ 510-511. Parties to the Framework have taken different positions on whether all VoIP traffic is currently interstate for jurisdictional purposes — and, therefore, within the Commission's authority under section 201 — and no party intends to change its position by joining this filing. Regardless of what the Commission has done in the past, however, it clearly has authority to hold that, going forward, all VoIP traffic is inseverable and, therefore, interstate for jurisdictional purposes. Indeed, the Commission has authority to hold — in light of dramatic technological and marketplace changes in recent years — that *all* traffic routed to or from the PSTN is now inseverable as a practical matter.

a. The Commission can hold that the communications landscape has changed dramatically in the past decade and now bears little resemblance to the world Congress faced when it enacted the 1996 Act.

The Commission can find that today, an ever greater proportion of calls are in IP format, as millions of consumers and businesses opt for IP-based offerings. As of December 2010, there were nearly 24 million cable voice subscribers — who generally receive VoIP service — a 22 percent increase since 2008, and a more-than-fourfold increase since 2005.[18] Over-the-top VoIP providers are also an increasingly attractive option for consumers; Vonage has approximately 2.5 million subscribers, and consumers can use services such as Skype and Google to make VoIP-

[18] *See* NCTA, *Industry Data: Operating Metrics (as of Dec. 2010), available at* http://www.ncta.com/Statistics.aspx (citing SNL Kagan); NCTA, *Cable Phone Customers 1998-2010*, *available at* http://www.ncta.com/Stats/CablePhoneSubscribers.aspx (citing SNL Kagan).

originated calls to any wireless or wireline phone.[19] Incumbent LECs, too, are rapidly deploying innovative new VoIP services.

The Commission can find that VoIP services increasingly upend the traditional idea of location-based and device-based phone numbers, including by enabling customers to have a single number — one of their choice and that may have no connection to their residence or billing address — that reaches them, no matter where they are and what phone (or computer or other device) they are using. These services also offer integrated packages of features and capabilities, allowing customers to perform multiple communications simultaneously while also accessing information on the Internet.[20]

In addition, consumers continue to flock to wireless services. As of December 2010, 96 percent of U.S. consumers had a wireless phone, and more than 29 percent of households had completely "cut the cord."[21] Consumers now spend 2.2 trillion minutes per year on their wireless phones, which far exceeds the number of wireline minutes.[22] The Commission can find that, like VoIP services, wireless services break the connection between telephone numbers and geography, through the mobility inherent in such services. Wireless providers are also deploying

[19] *See* Comments of Verizon and Verizon Wireless, *Connect America Fund*, WC Dkt. Nos. 10-90 *et al.*, at 7-8 (FCC Apr. 1, 2011) (citing statistics about the tremendous growth of both interconnected and over-the-top VoIP services); *see also* Comments of AT&T on NBP PN #25, *A National Broadband Plan for Our Future*, GN Dkt. Nos. 09-51 *et al.*, at 9 (FCC Dec. 22, 2009) ("AT&T PN #25 Comments").

[20] *See Vonage Order* ¶ 25 n.93 (noting that "integrated capabilities and features" are "inherent features of most, if not all, IP-based services"); *id.* ¶ 32.

[21] *See* Stephen Blumberg & Julian Luke, National Center for Health Statistics, *Wireless Substitution: Early Release of Estimates from the National Health Interview Survey* (June 8, 2011), at 6, *available at* http://www.cdc.gov/nchs/data/nhis/earlyrelease/wireless201106.pdf; CTIA, Wireless Quick Facts, *available at* http://www.ctia.org/advocacy/research/index.cfm/aid/10323.

[22] *See id.*; *see also* Robert Roche and Lesley O'Neill, *CTIA's Wireless Industry Indices, Semi-Annual Data Survey Results*, Chart 58 and Chart 59 (May 2009).

third- and fourth-generation wireless networks, which give consumers the ability — much like IP-based wireline services — to engage in simultaneous voice and data communications.

The flip side of this massive growth in intermodal services is a comparably large decline in traditional wireline services.[23] Between 2000 and 2008, the number of ILEC end-user switched access lines fell by 34 percent, and total ILEC interstate switched access minutes declined by a staggering 44 percent.[24] Traditional wireline carriers are also responding to competition from wireless and VoIP providers by offering their own geography-independent services, including any-distance, unlimited calling plans. Wireline carriers are also introducing facilities-based VoIP services, which will offer customers an integrated, any-distance communications service.[25]

b. The Commission can hold that, as consumers increasingly adopt any-distance, geography-independent services, it will become even more difficult for carriers to separate traffic into legacy intrastate and interstate categories for intercarrier compensation purposes.

Carriers historically relied on telephone numbers to determine the jurisdiction of wireline calls, not because telephone numbers determine jurisdiction, but because they were an easily ascertained and reliable proxy for the end points of a call. Customers had little, if any, choice

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[23] *See generally* AT&T PN #25 Comments at 8-13 (explaining that "[i]n view of the range of alternatives for voice service — many of which offer distinct advantages over traditional landline service — it is not surprising that the POTS business model is in a precipitous decline"); *see also 2011 NPRM* ¶ 503 (noting the decline in ILEC switched access minutes as a result of "competition and technological advances and the proliferation of alternate means of communicating").

[24] *See* FCC Industry Analysis and Technology Division, *Trends in Telephone Service* Table 10.1 (Sept. 2010) (showing 315.7 billion ILEC interstate switched access minutes in 2008 and 566.9 billion minutes in 2000); *id.* Table 8.1 (showing 179.6 million ILEC end-user switched access lines in June 2000 and 118.5 million lines in December 2008).

[25] *See* FiOS Digital Voice, *available at* http://www22.verizon.com/residential/homephone/fiosdigitalvoice (offering VoIP service that has "brilliant clarity" and is "completely integrated" with Verizon's FiOS service).

over the area code and first three digits of their telephone numbers (the "NPA-NXX"), and carriers routinely assigned customers telephone numbers with NPA-NXXs associated with the particular switch that provided dial-tone service to those customers. Telephone numbers were never a perfect proxy for geography,[26] but only minor tweaks to federal and state access charge regimes were required to account for discrepancies.

The advent of location-independent services — such as wireless services and nomadic VoIP — has challenged carriers' ability to use telephone numbers as a "proxy for . . . subscribers' geographic locations when making or receiving calls" — that is, for the end points of a voice communication. *Vonage Order* ¶ 26. Those services allow customers to make or receive calls from the same telephone number from anywhere, worldwide. The availability of "pick-your-own-area-code" services — which may also provide mobility — further divorces a customer's assigned telephone number from her physical location. Moreover, "find-me/follow-me" and "simultaneous ring" services offered by VoIP providers enable a call to a single number to ring on multiple phones (or other devices, such as computers and tablets) in multiple locations. And the intermodal porting of telephone numbers that were previously associated with a traditional wireline service adds an additional layer of complexity, as some of the numbers in a block of 1,000 or 10,000 numbers can now make or receive calls from anywhere, not just from the wire center where those numbers are traditionally homed. These services may stretch or, in

[26] *See* Memorandum Opinion and Order, *Access Billing Requirements for Joint Service Provision*, 4 FCC Rcd 7183, ¶¶ 21-26 (1989); Memorandum Opinion and Order, *Amendment of Part 69 of the Commission's Rules*, 102 F.C.C.2d 1243, ¶ 28 (1985); Memorandum Opinion and Order, *MTS and WATS Market Structure*, 97 F.C.C.2d 834, ¶ 108 (1984).

some cases, break the connection between the assigned telephone number and the geographic end points of a call, as they were designed to do.[27]

Even when telephone numbers still provide a meaningful proxy for geography, they may not provide a complete picture of the geography of an IP-based communication for jurisdictional purposes. Consumers are now using innovative, "multifaceted" IP-based services — including wireless services — that offer a "suite of integrated capabilities and features" that allows them "to perform different types of communications simultaneously." *Id.* ¶¶ 7, 23, 25, 32. Such services have challenged the traditional notion that a communication only has two end points. Indeed, certain VoIP services are designed "to *overcome* geography, not track it." *Id.* ¶ 25 (emphasis added).

In light of marketplace developments, the Commission can find that certain providers of any-distance, location-independent services have no *service-driven* incentive to develop the capabilities to enable innovative new services to be shoehorned into legacy regulatory classifications. It can also follow this finding with an affirmation of the Eighth Circuit's conclusion that service providers are not required to "develop a mechanism for distinguishing between interstate and intrastate communications merely to provide state commissions with an intrastate communication they can then regulate." *Minnesota PUC*, 483 F.3d at 578; *see also Vonage Order* ¶¶ 25, 29 (noting that it would "serve no legitimate policy purpose" to "impose substantial costs" on a nomadic VoIP provider to make specified changes simply "for certain

[27] *See, e.g., Vonage Order* ¶¶ 18, 23 (noting that there is no "practical means" or "plausible approach to separating" Vonage calls "into interstate and intrastate components for purposes of enabling dual federal and state regulations to coexist"); *Local Competition Order* ¶ 1044 (noting that, in light of the inherent mobility of wireless services, it is often "difficult for CMRS providers to determine, in real time . . . the customer's specific geographic location" for ratemaking purposes).

regulatory purposes," where they have "no service-driven reason to incorporate such capabilit[ies] into [their] operations").

c. In sum, the Commission can hold that, for *all* types of traffic, the practical and economic impediments to ensuring that a carrier applies its intrastate charges only to intrastate traffic provide the Commission with ample grounds for finding that *all* traffic routed to or from the PSTN is now inseverable as a practical matter.[28]

3. Continued State Regulation of Intercarrier Compensation Would Pose a Direct Obstacle to the Accomplishment of the Commission's Longstanding Policy Goals

It is equally clear that state intercarrier compensation regimes that vary from the uniform, federal regime would pose a direct obstacle to the strong federal policy in favor of *uniform* intercarrier compensation rates. Genuine intercarrier compensation reform cannot succeed for *any* class of traffic — including traffic over which the Commission has undisputed jurisdiction — unless the reforms encompass *every* class of traffic. Otherwise, artificial rate disparities for functionally substitutable services will continue to destabilize the industry as a whole. Preemption of state intercarrier compensation regimes that vary from the uniform federal regime is therefore necessary to prevent methodological inconsistencies from "thwart[ing] the lawful exercise of federal authority over interstate communications." *Vonage Order* ¶ 15; *see also National Ass'n of Regulatory Util. Comm'rs v. FCC*, 880 F.2d 422, 429 (D.C. Cir. 1989) ("*NARUC III*").

a. As shown above, the Commission has jurisdiction under sections 201 and 332(c) over a significant portion of traffic routed to or from the PSTN. *See* 47 U.S.C. §§ 201, 332(c). In the exercise of that federal-law authority, the Commission has long had a "goal" of

[28] That finding would apply with equal force to originating access, terminating access, and other intercarrier compensation rates.

"develop[ing] a uniform regime for all forms of intercarrier compensation."[29] That uniformity is "competitively and technologically neutral" and "is consistent with the pro-competitive de-regulatory environment envisioned by the 1996 Act," which requires "minimal regulatory intervention and enforcement." *2005 FNPRM* ¶ 33. The D.C. Circuit, moreover, has upheld a Commission decision that was based on these " 'policies favoring a unified compensation regime,' " explaining that it is "not for th[e] court[s] to second-guess the conclusion reached by the agency that Congress has entrusted with balancing those policies." *In re Core Communications, Inc.*, 455 F.3d 267, 283 (D.C. Cir. 2006) (citation omitted).

The Commission has also recognized the importance of ensuring that "carriers have [the] incentive to compete . . . on [the] basis of quality and efficiency," rather than "on the basis of their ability to shift costs to other carriers," which creates "troubling distortion[s] that prevent[] market forces from distributing limited investment resources to their most efficient uses." *ISP Remand Order* ¶ 4. These distortions "create[] incentives for inefficient entry" by carriers intent on taking advantage of "opportunit[ies] for regulatory arbitrage," rather than engaging in the kind of "telephone competition[] [that] Congress had intended to facilitate with the 1996 Act." *Id.* ¶ 21. And the Commission, applying section 706 of the 1996 Act, has recognized the importance of "promot[ing] the timely and comprehensive deployment of broadband facilities" in areas where broadband is not currently being deployed.[30]

[29] Notice of Proposed Rulemaking, *Developing a Unified Intercarrier Compensation Regime*, 16 FCC Rcd 9610, ¶ 97 (2001) ("*2001 NPRM*"); *see also 2005 FNPRM* ¶ 33 (expressing the Commission's goal of "a regime that would apply [intercarrier compensation] rates in a uniform manner for all traffic"); *2011 NPRM* ¶ 495 (noting that a "fundamental problem[]" with the current ICC regime is that "rates vary based on the type of provider and where the call originated, even though the function of originating or terminating the call does not change").

[30] Memorandum Opinion and Order, *Petition for Forbearance of the Verizon Telephone Companies*, 19 FCC Rcd 21496, ¶¶ 6, 34 (2004); *see also* FCC, *Connecting America: The*

Any situation with non-uniform intercarrier compensation rates — such as myriad rates for intrastate traffic and an otherwise-uniform federal default rate for all other traffic — would pose a significant obstacle to those federal policies. The Commission has emphasized that the current "patchwork of rates and regulations is inefficient" and "wasteful," because, where "opportunities for regulatory arbitrage" exist, "parties will revise or rearrange their transactions to exploit a more advantageous regulatory treatment, even though such actions, in the absence of regulation, would be viewed as costly or inefficient."[31] In other words, "regulatory uncertainty . . . as well as a lack of uniform rates, may be hindering investment and the introduction of new IP-based services and products." *National Broadband Plan* at 142.[32]

If existing state regimes for intrastate traffic were to remain alongside a new federal compensation regime, carriers would have the same incentives as today to engage in traffic pumping schemes to charge higher intrastate rates, rather than the new, lower federal default rate. *See 2011 NPRM* ¶ 40 (noting that "wasteful attempts to game the system will likely persist as long as ICC rates remain disparate and well above carriers' incremental costs of terminating a call"). And carriers would continue to have the incentive both to disguise traffic that remains subject to charges for intrastate traffic in an effort to pay only the lower federal default rate, and to claim an entitlement to payment at higher intrastate rates for traffic that is legitimately subject

National Broadband Plan at 142 ("*National Broadband Plan*") (noting that "[t]he current per-minute ICC system was never designed to promote deployment of broadband networks").

[31] *2011 NPRM* ¶¶ 502, 504; *2001 NPRM* ¶¶ 11-12; *see also National Broadband Plan* at 142 (noting that, as a result of ICC-related "arbitrage opportunit[ies]," "investment is directed to free conference calling and similar schemes for adult entertainment that ultimately cost consumers money, rather than to other, more productive endeavors" such as broadband deployment) (footnote omitted); *2005 FNPRM* ¶ 3 (noting that the availability of different rates for different types of traffic "create[s] both opportunities for regulatory arbitrage and incentives for inefficient investment and deployment decisions").

[32] To be sure, some carriers are deploying broadband in high-cost areas despite the uncertainty and lack of uniformity that characterize the current intercarrier compensation regime.

to the new federal default rate. Arbitrage efforts and outright fraud, designed to exploit the distinctions in the federal and state regimes, would necessarily undermine the uniform federal intercarrier compensation regime and the federal policies favoring efficiency, economic competition, and broadband deployment that a uniform intercarrier compensation regime furthers.

In addition, if state regimes were to permit carriers to increase originating access and other intercarrier compensation rates above their current levels, carriers could use those rates to evade the Commission's uniform default rule for terminating traffic. That is, carriers could seek to use those other rates to recoup revenues lost through the Commission's reduction of terminating rates to a uniform, default level, thereby undermining key benefits of the reduction of those rates. When the Commission capped rates for certain dial-up ISP traffic, it similarly adopted additional rules — the growth cap and the new markets rule — to ensure that its "efforts to limit intercarrier compensation" were "not undermine[d]." *ISP Remand Order* ¶ 86.

b. In light of these clear and longstanding federal policies, the Commission plainly has authority to preempt state intercarrier compensation rules that differ from the uniform federal default rate.

Under the Supremacy Clause of the Constitution, state law is preempted where, as here, it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" or a federal agency exercising delegated authority. *Hines v. Davidowitz,* 312 U.S. 52, 67 (1941); *United States v. Locke*, 529 U.S. 89, 109-10 (2000) ("In this context, [federal agency] regulations are to be given pre-emptive effect over conflicting state laws."). The Supreme Court has expressly found, in the context of this Commission's regulations, that "[t]he statutorily authorized regulations of an agency will pre-empt any state or local law that conflicts with such regulations or frustrates the purposes thereof." *City of New York v. FCC*, 486 U.S. 57, 64 (1988).

The Commission's determination that disparate state regimes pose an obstacle to federal intercarrier compensation policies and the new federal default rate is entitled, at a minimum, to "some weight." *Geier v. American Honda Motor Co.*, 529 U.S. 861, 883 (2000). Where Congress has delegated to an agency the "authority to implement the statute; the subject matter is technical; and the relevant history and background are complex and extensive" — all factors present in the context of intercarrier compensation — the agency's view that state law would "'stan[d] as an obstacle to the accomplishment and execution'" of the agency's "own regulation and its objectives" "make[s] a difference," as the agency is "'uniquely qualified' to comprehend the likely impact of state requirements." *Id.* (citations omitted).

In an analogous situation, the D.C. Circuit recognized the Commission's authority to preempt state laws that pose an obstacle to federal policies or, in the court's words, "negate[] the exercise by the [Commission] of its own lawful authority over interstate communication." *NARUC III*, 880 F.2d at 429. In that case, the Commission had adopted the policy of "encourag[ing] competition in the provision, installation, and maintenance of inside wiring," which the court found to be "consistent with the goals of the Act." *Id.* The court recognized further that "certain otherwise legitimate state actions regulating intrastate telephone service could interfere with the Commission's achievement of its valid goal of providing interstate telephone users with the benefits of a free market and free choice in the installation and maintenance of inside wiring." *Id.* at 430. The Commission therefore had authority to "take appropriate measures in pursuit of that goal," including issuance of a "valid . . . preemption order" with respect to state regulation that "would necessarily thwart or impede the operation of a free market." *Id.*[33]

c. Nothing in section 2(b) prevents the Commission from preempting state regimes where the Commission finds that the "state's exercise of [such] authority" would "negate[] the exercise by the [Commission] of its own lawful authority" over intercarrier compensation for "interstate communication[s]," and would frustrate important federal policy objectives with respect to competition and efficient investment in new technologies and services.[34] More generally, because conflict preemption "turns on the identification of [an] 'actual conflict,' " it operates even in the face of a savings provision, such as section 2(b), because courts "can assume that Congress or an agency ordinarily would not intend to permit a significant conflict." *Geier*, 529 U.S. at 884-85 (citation omitted); *see also Crosby v. National Foreign Trade Council*, 530 U.S. 363, 387-88 (2000) ("[T]he existence of conflict cognizable under the Supremacy Clause does not depend on express congressional recognition that federal and state law may conflict.").

In any event, the scope of section 2(b) has shrunk significantly, and it will continue to shrink as dramatic technological and marketplace changes increasingly blur the distinction between "interstate" and "intrastate" traffic. As explained above, a large and rapidly increasing percentage of voice calls are now made using all-distance services that challenge legacy jurisdictional distinctions.

[33] Although the D.C. Circuit found that the Commission had not fully explained the basis for its preemption decision, *see NARUC III*, 880 F.2d at 431, the Commission did so soon thereafter, and no party sought review of the Commission's more detailed explanation of its decision to preempt state regulation regarding inside wiring, *see* Third Report and Order, *Detariffing the Installation and Maintenance of Inside Wiring*, 7 FCC Rcd 1334 (1992).

[34] *NARUC III*, 880 F.2d at 429; *see PSC of Md.*, 909 F.2d at 1514-15 (rejecting similar argument based on section 2(b)).

d. Recent Supreme Court and court of appeals decisions buttress the Commission's authority to preempt state regulations that pose an obstacle to the strong federal policy in favor of uniform intercarrier compensation rates, and they confirm that a Commission decision preempting state authority over intercarrier compensation rates would be upheld on review.

In *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1753 (2011), the Supreme Court held that the "'liberal federal policy'" in favor of arbitration could preempt even general provisions of state law that "'stand[] as an obstacle to the accomplishment and execution'" of a federal policy. *Id*. at 1749, 1753 (citations omitted). Like the Communications Act, the Federal Arbitration Act reserved some role for the states, by preserving state-law contract defenses "as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. The Court nonetheless found the state law at issue to be preempted because it "interfere[d] with fundamental attributes" of the federal policy and "create[d] a scheme inconsistent" with that policy. *Concepcion*, 131 S.Ct. at 1748. Preserving state regulation of intercarrier compensation rates for "intrastate" traffic would similarly create a regime "inconsistent" with the "fundamental attributes" of a *uniform* intercarrier compensation system, thus hindering the Commission's longstanding goals of eliminating arbitrage opportunities and promoting broadband deployment.

In *PLIVA, Inc. v. Mensing*, 131 S. Ct. 2567, 2577 (2011), the Supreme Court found state common-law claims against generic drug manufacturers to be preempted because it was "'impossible . . . to comply with both state and federal requirements.'" (Citation omitted.) The Court noted that "[i]t was not lawful under federal law for the Manufacturers to do what state law required of them," because the tort claims sought to require stronger warnings that would have been *prohibited* by federal law. *Id.* The same would be true if state commissions set rates higher than the uniform federal default rate. In such circumstances, federal law would *forbid* conduct that state law *required* — namely, charging more than the uniform federal rate — and the higher state rates would accordingly be preempted.

In *Farina v. Nokia Inc.*, 625 F.3d 97 (3d Cir. 2010), *cert. pending*, the Third Circuit held that state common-law claims alleging harm from radio frequency emissions posed an obstacle to the Commission's regulation of wireless services and were therefore preempted. When an agency is charged with "balancing competing objectives," it has authority "to use its reasoned judgment to weigh the relevant considerations and determine how best to prioritize between these objectives." *Id.* at 123. Legal standards that "vary from state to state" would allow each state to "re-balanc[e]" those considerations, and would "eradicate[e] the uniformity necessary to regulating the wireless network." *Id.* at 123-26. The Commission's rules regarding intercarrier compensation similarly require a balancing of multiple policy goals — including promoting broadband deployment, reducing implicit support systems, and eliminating arbitrage opportunities — and any state attempt to impose a different regime would necessarily involve "re-balancing" those factors in a different way, in conflict with the Commission's reasoned policy judgments.

In *Whistler Investments, Inc. v. Depository Trust and Clearing Corp.*, 539 F.3d 1159 (9th Cir. 2008), the Ninth Circuit noted that Section 17A of the Exchange Act was enacted to "replac[e] an inefficient and outmoded system of clearing agencies," and the Securities and Exchange Commission was given authority "to regulate and control a *national system* for clearing and settling securities transactions." *Id.* at 1166-67 (emphasis added).[35] Because the SEC had specifically approved certain procedures for settling securities transactions, any state-

[35] *See also Chae v. SLM Corp.*, 593 F.3d 936, 945 (9th Cir. 2010) (holding that state-law claims challenging the terms of federal student loans posed an obstacle to federal policy because "the possibility of similar claims being asserted under varying state laws in each of the fifty states . . . would impair and threaten the efficacy of the federal lending effort for students").

law claims challenging those procedures conflicted with federal law and were thus preempted. *See id.* at 1166-68. The Framework's intercarrier compensation reforms also involve "replacing an inefficient and outmoded" system with a "more modern and efficient" regulatory scheme, and any continued state regulation of intercarrier compensation rates would only undermine the uniformity that is essential to the achievement of the Commission's longstanding policy goals.

* * *

In sum, both criteria for application of the inseverability doctrine are easily satisfied here. The Commission can find that dramatic marketplace and technological changes have both blurred the lines between "interstate" and "intrastate" traffic, and it is no longer practical to distinguish between such traffic and afford it different treatment for pricing and billing purposes. Any state attempts to regulate the "intrastate" component of such traffic would inevitably interfere with the accomplishment of the Commission's longstanding policy objectives with respect to intercarrier compensation. The Commission may thus adopt a uniform default rate for *all* traffic routed on the PSTN and, in turn, preempt any state regimes that vary from the uniform federal scheme.

C. The Commission Has Authority To Select $0.0007 Per Minute as the Uniform Default Rate

1. Selecting $0.0007 per minute as the uniform default rate for all traffic routed to or from the PSTN would clearly be reasonable. As a result of the Commission's "mirroring" rule, that is *already* the default rate for a substantial portion of the traffic that carriers exchange today (such as wireless and ISP-bound traffic). *See ISP Remand Order* ¶ 89. When the Commission adopted that rate in the *ISP Remand Order*, it drew upon some then-recently negotiated interconnection agreements, which showed a "downward trend in intercarrier compensation rates." *Id.* ¶ 85. The $0.0007 per minute rate is also consistent with the rates contained in certain recently negotiated agreements between ILECs and CLECs. For example, Verizon recently entered into a commercial agreement with Bandwidth.com for the exchange of VoIP traffic at $0.0007 per minute. *See also* Comments of Verizon and Verizon Wireless, *Developing a Unified Intercarrier Compensation Regime*, WC Dkt. Nos. 05-337 *et al.*, at 49-50 (FCC Nov. 26, 2008) (noting that Verizon and Verizon Wireless have entered into agreements with a number of carriers — including pre-merger AT&T, Level 3, Comcast, and at least 25 CLECs — to exchange traffic at or below the $0.0007 per minute rate).

As the Commission has recognized, evidence that "carriers have agreed to rates" for intercarrier compensation through voluntary, arms-length negotiations is substantial evidence that those rates are just and reasonable, *ISP Remand Order* ¶ 85, and would thus satisfy both section 201(b) and, consistent with the discussion in section I.A.3 above, the pricing standards in section 252(d)(2). The Commission has also emphasized more generally that rates set through market-based negotiations are just and reasonable rates. *See*, *e.g.*, *ACS Anchorage Forbearance Order*[36] ¶¶ 39-40 & n.136 (finding that "commercially negotiated rates" provide "just and reasonable prices").[37] Similarly, the Commission has resolved "historically vexing issues" involving "interstate access reform" by adopting a negotiated agreement reached by a coalition of different providers that "negotiated with each other in good faith and fashioned a reasonable compromise that . . . addresses their competing interests."[38]

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[36] Memorandum Opinion and Order, *Petition of ACS of Anchorage, Inc., for Forbearance from Sections 251(c)(3) and 252(d)(1)*, 22 FCC Rcd 1958 (2007) ("*ACS Anchorage Forbearance Order*").

[37] *See also* Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, 18 FCC Rcd 16978, ¶ 664 (2003) (finding that "arms-length agreements" demonstrate that the rate is "just and reasonable").

[38] Sixth Report and Order, *Access Charge Reform*, 15 FCC Rcd 12962, ¶¶ 1-2, 48 (2000) ("*CALLS Order*").

Courts have similarly held that, in competitive markets, the Commission may "conclude that market forces generally will keep prices at a reasonable level." *Illinois Pub. Telecomms. Ass'n v. FCC*, 117 F.3d 555, 562 (D.C. Cir. 1997).[39] The Supreme Court recently reaffirmed that the *Mobile-Sierra* doctrine — which applies to the Communications Act[40] — requires an agency to "presume that the rate set out in a freely negotiated . . . contract meets the 'just and reasonable' requirement imposed by law." *Morgan Stanley Capital Group Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty.*, 554 U.S. 527, 530 (2008).

2. Adopting a uniform default rate of $0.0007 per minute for all traffic, regardless of provider or technology, would be well supported by the Commission's prior treatment of wireless providers. In 1996, wireless was still emerging as a relatively new technology with great promise. In implementing the 1996 Act, the Commission chose *not* to saddle wireless carriers with the costs of the existing intercarrier compensation system. Instead, the Commission decided that all calls between wireless carriers and LECs that originate and terminate in the same MTA — broad areas that cover large swaths of one or more states[41] — would be subject to the new, lower reciprocal compensation rates rather than the higher tariffed access charge rates that applied to wireline calls that cross traditional exchange and state boundaries. *See Local Competition Order* ¶ 1036; 47 C.F.R. § 51.701(b)(2). Because the majority of wireless traffic involves intraMTA calls, this decision significantly insulated wireless carriers from the inefficiencies and implicit support systems that plague the legacy intercarrier compensation regime.

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[39] *See also Elizabethtown Gas Co. v. FERC*, 10 F.3d 866, 870 (D.C. Cir. 1993) (holding that an agency "may rely upon market-based prices . . . to assure a 'just and reasonable' result").

[40] *See, e.g.*, *Western Union Tel. Co. v. FCC*, 815 F.2d 1495, 1501 (D.C. Cir. 1987).

[41] FCC, The Major Trading Areas (MTAs), *available at* http://wireless.fcc.gov/auctions/data/maps/mta.pdf.

In 2001, the Commission's "'mirroring' rule" further reduced the rates paid by wireless carriers for intraMTA calls. Under the mirroring rule, incumbent LECs that took advantage of the Commission's rate caps on dial-up ISP traffic — as many of them did shortly after the release of the *ISP Remand Order* — were required to offer to apply those same rates to intraMTA traffic exchanged with wireless carriers. *See ISP Remand Order* ¶ 89. The wireless carriers uniformly accepted that offer, and the majority of intraMTA traffic has now been exchanged for years at rates at or below $0.0007 per minute.

D. The Commission Has Authority To Adopt Reasonable Interim Rules To Ease the Transition to a Unified Intercarrier Compensation Regime

A critical aspect of the Framework is the transitional mechanism from the current, badly broken intercarrier compensation regime to a uniform default rate of $0.0007 per minute for all traffic, regardless of provider or technology. In the first stage of reform, intrastate rates will be reduced by 50 percent of the difference between intrastate and interstate rates. One year after that, all access rates will be unified at the interstate rate. In the second stage of reform, both access and reciprocal compensation rates will be phased down in a series of steps to the end-state default rate of $0.0007 per minute.[42]

The D.C. Circuit has recognized that the Commission must be accorded substantial leeway in crafting transitional mechanisms, as the line-drawing required in making those judgments "amount[s] to a policy decision" that the agency is uniquely equipped to make.

[42] The Framework also proposes an interim rule under which VoIP traffic exchanged with LECs would initially be rated at either reciprocal compensation or interstate access rates, and would not be subject to intrastate access rates. The rates applicable to VoIP traffic, as with all other traffic on the PSTN, would decline and converge over time to $0.0007 per minute. This aspect of the Framework falls within the Commission's traditional authority, discussed in the text, to adopt interim or transitional rules; it is also supported by the potential for the Commission to find, going forward, that VoIP traffic is inseverable and, therefore, interstate for jurisdictional purposes.

PSWF Corp. v. FCC, 108 F.3d 354, 358 (D.C. Cir. 1997).[43] There is "no legal basis for concluding that some [other line] would clearly have been preferable," so long as the one the agency chooses is a reasonable attempt to accommodate opposing concerns. *Id.* Indeed, the D.C. Circuit has rejected the claim that a bright-line transitional rule was arbitrary where, as here, the Commission "balanced the need to implement the new regulatory regime against the effect of upsetting . . . expectations" and "reasonably feared" that adopting a different balance "would diminish the efficiency gains expected from" its new regime. *Bachow Communications, Inc. v. FCC*, 237 F.3d 683, 686 (D.C. Cir. 2001) (affirming transitional rules for allocation of fixed wireless communications licenses).

In a variety of different contexts — including intercarrier compensation — the Commission has found it appropriate to adopt transitional mechanisms that advance its policy goals, while avoiding "a market-disruptive 'flash cut'" to the end state of the new policy regime. *ISP Remand Order* ¶¶ 77-78 (adopting transitional mechanism that gradually lowered the intercarrier compensation rate for ISP-bound traffic over a 36-month period). Courts have repeatedly upheld the Commission's authority in this regard. As the D.C. Circuit has explained, "[a]voidance of market disruption pending broader reforms is, of course, a standard and accepted justification for a temporary rule." *Competitive Telecomms. Ass'n v. FCC,* 309 F.3d 8, 14 (D.C. Cir. 2002); *see also Texas Office of Pub. Util. Counsel v. FCC*, 183 F.3d 393, 437 (5th Cir. 1999) ("*TOPUC I*") (deferring to the Commission's "reasonable judgment about what will constitute 'sufficient' support during the transition period from one universal service system to another");

[43] *See also Competitive Telecomms. Ass'n v. FCC,* 117 F.3d 1068, 1073-74 (8th Cir. 1997) ("Although temporary agency rules are subject to judicial review notwithstanding their transitory nature, 'substantial deference by courts is accorded to an agency when the issue concerns interim relief.'") (quoting *MCI Telecomms. Corp. v. FCC*, 750 F.2d 135, 140 (D.C. Cir. 1984)).

Community Television, Inc. v. FCC, 216 F.3d 1133, 1142 (D.C. Cir. 2000) (affirming transitional mechanism for migration from analog to digital television where the Commission "reasonably balanced competing demands for spectrum" and "adequately addressed the equitable concerns" of companies that would be affected by the transition).

Under this precedent, the Commission plainly has authority to set interim rates — including the interim rates that carriers could charge to terminate VoIP traffic — to establish a rational glide path from today's fragmented intercarrier compensation regimes to a uniform default rate of $0.0007 per minute. A transitional mechanism that gradually reduces and unifies intercarrier compensation rates over a five-year period strikes a reasonable balance between the need to eliminate wasteful arbitrage opportunities and the need to avoid making an immediate "flash cut" to the new regime.

E. The Commission Has Authority To Increase the Cap on Subscriber Line Charges and Create a Temporary Access Replacement Mechanism as Part of Its Broader Reform Efforts

The Framework proposes two key opportunities for access revenue recovery for carriers that may face reduced intercarrier compensation revenues as a result of the Framework: (1) a modest increase in the subscriber line charges ("SLCs") that carriers may impose; and (2) a temporary access replacement mechanism for carriers that face a net loss of intercarrier compensation revenue as a result of the Framework and are unable to recoup that revenue through SLC increases. The Commission has ample legal authority to adopt each of those measures.

1. The Framework would permit — but not require — carriers to increase their SLCs by up to $0.75 per year (or up to $0.50 per year if they choose to avail themselves of the access replacement mechanism described below). The Commission clearly has authority to take this step. In connection with prior reforms of the intercarrier compensation regime, the Commission has permitted carriers to increase SLCs to compensate for other lost revenue, and the courts affirmed that decision.

In the *CALLS Order*, the Commission adopted an industry-wide proposal for reform of the marketplace for interexchange services. One component of that plan was elimination of Presubscribed Interexchange Carrier Charges ("PICC"), which were fixed fees that LECs imposed on an end user's interexchange carrier. *See CALLS Order* ¶ 19. Those charges "created market inefficiencies," both because, in recovering such fees from end users, IXCs charged residential customers "more than the costs IXCs have incurred for providing them service," and because the charges were "not assessed directly on consumers," but rather were subject to averaging and mark-ups by IXCs, which prevented consumers from comparing different carriers' prices. *Id.* To offset lost revenue from the elimination of the PICC, the Commission raised the SLC cap, relying on its authority under sections 4(i) and 201 to 205 of the Act. *Id.* ¶ 76 n.120. The Commission found that this rate restructuring "simplifies the current rate structure, moves towards cost-based rates," "eliminat[es] some of the complexities involved in the administration of current Commission rules and provid[es] greater opportunities for pricing flexibility." *Id.* ¶ 81.

The Fifth Circuit affirmed the *CALLS Order* in relevant part, holding that "the increase in the SLC cap represents [the Commission]'s reasoned attempt to maintain the difficult balance between the principles of ensuring affordability and encouraging competition." *Texas Office of Pub. Util. Counsel v. FCC*, 265 F.3d 313, 322 (5th Cir. 2001) ("*TOPUC II*"). In particular, the court deferred to the Commission's determination that the "pro-competitive benefits from the abolition of the PICC would offset any increase in the SLC." *Id.* at 323. Indeed, because the

SLC is "imposed directly against [] consumers" — and because no carrier was *required* to charge an SLC — "competitive pressure could force ILECs to reduce the SLC through efficiency gains." *Id.*; *see also National Ass'n of State Util. Consumer Advocates v. FCC*, 372 F.3d 454, 459-61 (D.C. Cir. 2004) (rejecting various statutory and APA challenges to the Commission's decision to increase the SLC cap).

The same is true of an increase in the SLC cap in connection with the Framework. Like the SLC increase in the *CALLS Order*, this would not be a freestanding policy change, but would be one component of a broader intercarrier compensation reform effort. Also like the *CALLS Order*, the SLC increase would not (as some may claim) provide a windfall to carriers, but would be designed to offset other revenue that was lost as a result of the Commission's reform efforts. Moreover, the proposal in the Framework merely involves *raising the cap* on the SLC. No carrier would be *required* to raise its rates — and in light of vigorous competition from VoIP, wireless, and cable providers, carriers may choose not to do so to the degree permitted. In sum, as the Fifth Circuit and D.C. Circuit have recognized, a modest increase in the SLC cap in connection with a broader reform effort falls comfortably within the Commission's discretion.

2. The Commission also has authority to create a temporary access replacement mechanism ("ARM"). The ARM would provide support to carriers that face a net loss of intercarrier compensation revenue as a result of the Framework and are unable to recoup that revenue through SLC increases. The ARM is purely a transitional mechanism, and would be phased out over three years after the $0.0007 rate is in place for all traffic.

The Commission can rely on several different sources of authority to create the ARM. At the outset, section 254(e) provides that any universal service support should be "explicit." 47 U.S.C. § 254(e); *see also CALLS Order* ¶ 193 (noting the Commission's "determinat[ion] that implicit support for universal service should be identified and removed from interstate access charges, and should be provided instead through explicit support mechanisms"). A key component of the Framework is the shift from the current intercarrier compensation regime — which contains significant implicit support — to a uniform regime, combined with *explicit* universal service support for broadband deployment in areas that are not currently being served. The Fund will advance the goals of section 254 by providing temporary, explicit support for certain carriers as intercarrier compensation rates — and the accompanying implicit support — are gradually reduced.

The *CALLS Order* also offers support for the Commission's authority to create a mechanism that offers carriers the ability to recover revenues that cannot be attained from SLC increases. In that order, the Commission — relying on section 254 of the 1996 Act — established "an explicit interstate universal service support mechanism that will provide support to replace $650 million of annual implicit support currently collected through interstate access charges, which is being phased out as part of the CALLS Proposal's common line restructuring." *CALLS Order* ¶ 195; *id.* ¶¶ 190-192 (discussing universal service principles). The mechanism adopted in the *CALLS Order* provided additional funding to carriers only "in areas where they are unable to recover their permitted revenues from the newly revised SLCs." *Id.* ¶ 195. Although the Fifth Circuit remanded the *CALLS Order* with respect to the *size* of the new explicit support mechanism, *see TOPUC II*, 265 F.3d at 327-28 — a size that subsequently was further justified and maintained by the Commission — no party challenged the Commission's authority to create the mechanism in the first instance, and the Fifth Circuit did not question the

Commission's ability to do so.[44] The ARM proposed in the Framework is actually far *narrower* than the explicit support mechanism at issue in the *CALLS Order*, both because the ARM in the Framework would be much smaller, and because it would have an automatic end date.

Finally, creation of the ARM is supported by the Commission's well-established authority, discussed above, to create reasonable transitional mechanisms in order to avoid "flash cuts" to new policies. *See supra* Section I.D. For certain carriers, the ARM is critical to the transition from the current regime to a uniform default rate, as it will prevent sharp, immediate decreases in intercarrier compensation revenue. At the same time, however, the ARM is only a *temporary* measure that will be phased out over three years after the $0.0007 rate is in place for all traffic. Both the size of the Fund and its duration necessarily involve line-drawing exercises — and a balancing of competing interests — that are well within the Commission's discretion, as long as the Commission reasonably explains why it chose to draw the lines in that manner.[45] *See Bachow Communications*, 237 F.3d at 686-87 (affirming bright-line transitional rules that "balanced the need to implement the new regulatory regime against the effect of upsetting . . . expectations" where the Commission "reasonably feared" that adopting a different balance "would diminish the efficiency gains expected from" its new regime).

[44] The court remanded the *CALLS Order* for "further analysis and explanation" of why the Commission specifically chose $650 million as the size of the Universal Service Fund. *TOPUC II*, 265 F.3d at 327-28. The court simply noted that the Commission must "provide some explanation as to why it found one study [regarding the proposed size of the fund] to be more persuasive than the other." *Id.* On remand, the Commission again selected $650 million as the support amount, and provided additional reasons for its decision. *See* Order on Remand, *Access Charge Reform*, 18 FCC Rcd 14976, ¶¶ 13-33 (2003). No party challenged that decision.

[45] In light of the *TOPUC II* decision, the Commission must exercise "independent judgment" about the size of the Fund. 265 F.3d at 328. That is, it must independently verify that the size of the transition Fund is reasonable, and may not simply "defer[] to private parties' estimates." *Id.*

II. THE COMMISSION HAS AMPLE AUTHORITY TO SUPPORT BROADBAND SERVICES WITH UNIVERSAL SERVICE FUNDING

The Framework calls for the creation of new universal service funding mechanisms that will support the deployment and operation of broadband infrastructure in high-cost areas. The Commission has clear authority to adopt such mechanisms. Section 254 of the 1996 Act (47 U.S.C. § 254) — interpreted in light of section 706 of the 1996 Act (*id.* § 1302) and section 6001 of the American Recovery and Reinvestment Act (*id.* § 1305) — gives the Commission direct authority to support broadband with universal service funding.

Section 254(b) directs the Commission to use federal universal service programs to promote access to information services. It mandates that "the Commission *shall* base policies for the preservation and advancement of universal service on" six principles, two of which concern access to information services. *Id.* § 254(b) (emphasis added). Specifically, section 254(b)(2) states that "[a]ccess to *advanced* telecommunications and *information services* should be provided in all regions of the Nation." *Id.* § 254(b)(2) (emphases added). And section 254(b)(3) provides that "[c]onsumers in all regions of the Nation, . . . should have access to telecommunications and *information services*, including interexchange services and *advanced* telecommunications and *information services*, that are reasonably comparable to those services provided in urban areas[.]" *Id.* § 254(b)(3) (emphases added). These principles clearly empower the Commission to use universal service funding to support broadband. Indeed, in today's world, "advanced telecommunications and information services" *is* broadband Internet access.

There is some tension between these principles and section 254(e), which states that "only an eligible telecommunications carrier designated under section 214(e) of this title shall be eligible to receive specific Federal universal service support." *Id.* § 254(e). Similarly, section 254(c)(1) provides that "[u]niversal service is an evolving level of *telecommunications* services[.]" *Id.* § 254(c)(1) (emphasis added). But these provisions are not sensibly read to bar the Commission from using universal service funding to support broadband.

To the contrary, section 254(c)(1) itself rejects a static focus on legacy technologies, defining "universal service" as an "*evolving* level of telecommunications services that the Commission shall establish periodically under this section, *taking into account advances* in telecommunications *and information technologies and services*." *Id.* (emphases added). The remainder of section 254(c) further confirms that universal service can encompass broadband. Section 254(c)(2) authorizes the Commission to "modif[y] . . . the definition of the *services* that are supported by Federal universal service support mechanisms." *Id.* § 254(c)(2) (emphasis added). This direction to "modif[y] . . . the definition" of universal service refers not to the "telecommunications services" that are to be supported, but more broadly to the "services" that are to be supported.

As the Commission explained in connection with section 254(h), which sets out the universal service framework for schools and libraries, "the varying use of the terms 'telecommunications services' and 'services' . . . suggests that the terms were used consciously to signify different meanings."[46] There, even though section 254(h) is entitled "*Telecommunications services for certain providers*," 47 U.S.C. § 254(h) (emphasis added), the Commission nonetheless concluded that the use of the broader term "services" in sections 254(h)(1)(B)[47] and 254(c)(3)[48] authorizes the Commission to support *non*-telecommunications

[46] Report and Order, *Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776 ¶ 439 (1997) ("*First Universal Service Order*").

[47] 47 U.S.C. § 254(h)(1)(B) provides, in relevant part: "All *telecommunications carriers* serving a geographic area shall, upon a bona fide request for any of *its services* that are within the definition of universal service under subsection (c)(3) of this section, provide *such services* to elementary schools, secondary schools, and libraries for educational purposes at rates less than the amounts charged for *similar services* to other parties." (Emphases added.)

services for schools and libraries. *First Universal Service Order* ¶¶ 436-439. Similarly, here, Congress's use of the same broad term "services" in section 254(c)(2) authorizes the Commission to "modif[y] . . . the definition" of universal service to include non-telecommunications services, even though section 254(c)(1) refers to "telecommunications services." 47 U.S.C. § 254(c)(1), (2).

At the very least, this language creates ambiguity about the reach of section 254.[49] The Fifth Circuit has applied *Chevron* deference in virtually identical circumstances. *See TOPUC I*, 183 F.3d 393. There, the court deferred to the Commission's determination that section 254 authorizes the Commission to direct universal service funding to Internet access and other non-telecommunications services for purposes of the schools and libraries program. *Id.* at 440, 442-43. The court recognized that the statutory language points both ways, *see id.* at 440-42, but found that section 254(c)(1) "invites the FCC periodically to re-define 'universal service' to 'tak[e] into account advances in telecommunications and information technologies and services.'" *Id.* at 442 (quoting 47 U.S.C. § 254(c)(1)). Other language in section 254(h) also "instructs the FCC to establish competitively neutral rules to 'enhance . . . access to advanced telecommunications and information services.'" *Id.* (quoting 47 U.S.C. § 254(h)(2)(A)). The court held that this language made the statute "ambiguous enough to require deference under *Chevron* step-two," and it affirmed the Commission's decision to extend universal service support to information services in the schools and libraries program. *Id.* at 440, 442-43. Here,

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[48] 47 U.S.C. § 254(c)(3) provides: "In addition to *the services* included in the definition of universal service under paragraph (1), the Commission may designate *additional services* for such support mechanisms for schools, libraries, and health care providers for the purposes of subsection (h) of this section." (Emphases added.)

[49] Several courts have held that the Commission's interpretation of section 254 is reviewable under *Chevron* step two. *See, e.g., Rural Cellular Ass'n v. FCC*, 588 F.3d 1095, 1101-02 (D.C. Cir. 2009); *Qwest Corp. v. FCC*, 258 F.3d 1191, 1200-02 (10th Cir. 2001).

too, sections 254(b) and 254(c)(1)-(2) create more than enough ambiguity to permit the Commission to direct universal service funding to broadband, regardless of any contrary suggestion in sections 254(c)(1) or 254(e).

Like many parts of the 1996 Act, section 254, with its apparently competing directives, is not "a model of clarity," but instead is "a model of ambiguity or indeed even self-contradiction." *Iowa Utils. Bd.*, 525 U.S. at 397. But that fact gives the Commission discretion to give section 254 its most rational meaning, consistent with the intentions and policy choices expressed by Congress. *See Akhtar v. Gonzales*, 450 F.3d 587, 595 (5th Cir. 2006) (deferring to agency's interpretation of a statute that contained conflicting indications of congressional intent); *National Ass'n of Cas. & Surety Agents v. Board of Governors of the Fed. Reserve,* 856 F.2d 282, 289-90 (D.C. Cir. 1988) (deferring to agency's "permissible reconciliation of the inherent tension of the statute"). A cramped reading of section 254 that fixates on the "telecommunications" language and ignores the "information services" language would improperly elevate the former over the latter in violation of congressional intent. It would also contradict provisions elsewhere in the 1996 Act that instruct the Commission to promote broadband and other advanced services. As the D.C. Circuit has explained, "statements of congressional policy can help delineate the contours of statutory authority,"[50] and here, at least two such statements make clear that the Commission has authority under section 254 to support information services with universal service funding.

First, section 706(a) of the 1996 Act provides that the Commission "shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all

[50] *Comcast Corp. v. FCC*, 600 F.3d 642, 654 (D.C. Cir. 2010).

Americans." 47 U.S.C. § 1302(a).[51] Section 706(b) further states that if the Commission finds that advanced telecommunications capability is not being deployed to all Americans, it "shall take immediate action to accelerate deployment of such capability" in those areas that lack access to broadband. *Id.* § 1302(b). Given the Commission's findings regarding the obstacles to deployment of broadband in high-cost areas, section 706 supports the Commission's authority under section 254 to fund broadband in those areas where broadband is not deployed and where it could not be economically provided without support. It would be nonsensical for Congress to direct the Commission to "take immediate action" to accelerate broadband deployment in section 706(b) while simultaneously prohibiting the Commission from funding broadband under section 254.

Second, the American Recovery and Reinvestment Act makes ubiquitous broadband deployment a key Commission goal and mandates that the Commission "shall seek to ensure that all people of the United States have access to broadband capability." *Id.* § 1305(k)(2). It also directs the Commission to develop "a detailed strategy for achieving affordability of such service." *Id.* § 1305(k)(2)(B). These statutory directives — which, like section 706, use mandatory "shall" language — make clear that Congress intended for the Commission to ensure that broadband service is deployed to all Americans.

In short, the Commission has ample authority under section 254 to support broadband in areas that are not currently being served. Nonetheless, to buttress its authority under that section, the Commission could forbear from sections 254(c)(1) and 254(e) or from other statutory provisions that limit universal service to "telecommunications" carriers or services. Indeed,

[51] Section 706(a) does not constitute an independent grant of statutory authority. Rather, it is a "statement[] of congressional policy" that counsels in favor of a broader reading of the Commission's authority under section 254. *Comcast*, 600 F.3d at 654.

section 706(a) of the 1996 Act expressly identifies "regulatory forbearance" as a key means of fulfilling the Commission's obligation to ensure ubiquitous access to broadband services.[52] Further, the D.C. Circuit already has upheld the Commission's use of forbearance to promote its national broadband goals. *See*, *e.g.*, *Ad Hoc Telecomms. Users Comm. v. FCC*, 572 F.3d 903, 907 (D.C. Cir. 2009) ("As contemplated by § 706, the FCC has utilized forbearance from certain Title II regulations as one tool in its broadband strategy.").

III. THE COMMISSION HAS AUTHORITY TO ELIMINATE OUTDATED SERVICE OBLIGATIONS THAT HINDER THE TRANSITION TO AN ALL-IP COMMUNICATIONS INFRASTRUCTURE

The Framework is designed to facilitate the transition from the legacy PSTN and plain-old telephone service ("POTS") to broadband infrastructure and IP-enabled communications. But the Commission cannot effect that transition if regulators continue to impose legacy service obligations — such as ETC and COLR mandates — that effectively require incumbent carriers (and only those carriers) to continue providing service, with or without support, throughout their territories, in some cases using outdated, circuit-switched TDM technology. Service obligations such as COLR requirements, which originally were imposed on telecommunications carriers as a means of ensuring universal service in a monopoly environment, are poorly suited to today's competitive communications ecosystem. Those obligations now *undermine* universal service by deterring carriers from deploying broadband and IP-enabled services. To achieve its broadband goals and effectively implement the Framework, the Commission can ensure that these anachronistic ETC and COLR obligations are fundamentally transformed or eliminated

[52] 47 U.S.C. § 1302(a) ("The Commission . . . shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans . . . by utilizing, in a manner consistent with the public interest, convenience, and necessity, price cap regulation, regulatory forbearance, measures that promote competition in the local telecommunications market, or other regulating methods that remove barriers to infrastructure investment.").

altogether. And it can take steps to ensure that any new broadband service obligations further, rather than hinder, the Commission's universal service goals.

A. Federal and State Legacy Service Obligations Undermine the Commission's Broadband Universal Service Goals

Section 214(e)(1) provides that ETCs "shall, throughout the service area for which the designation is received . . . offer the services that are supported by Federal universal service support mechanisms under section 254(c)[.]" 47 U.S.C. § 214(e)(1). The Commission has interpreted section 214(e)(1) as requiring an ETC to provide supported services throughout its service area *regardless of whether the ETC is receiving any high-cost support for providing such service*.[53] Under this interpretation, an ETC's obligation to "offer and advertise supported services 'throughout the service area for which the designation is received' . . . appl[ies] regardless of whether support is actually provided to ETCs operating within the designated area."[54]

Similarly, state public utility commissions in some cases still impose COLR obligations on incumbent LECs. These obligations generally require those carriers to provide telecommunications services to *all customers* in a given geographic area, with some exceptions, often at regulated rates.

In addition, a variety of other legacy service obligations at both the state and federal levels specify the *types* of services that carriers must offer throughout their service areas. In the

[53] *See, e.g.*, *First Universal Service Order* ¶ 192 (noting that an ETC's "service area" is the "overall area for which the carrier *may* receive support from federal universal service support mechanisms") (emphasis added).

[54] *2011 NPRM* ¶ 88 (quoting 47 U.S.C. § 214(e)(1)); *see also* Order, *High-Cost Universal Service Support*, 23 FCC Rcd 8834, ¶ 29 (2008) ("The Act does not . . . require that all ETCs must receive support, but rather only that carriers meeting certain requirements be *eligible* for support," and "designation as an ETC does not automatically entitle a carrier to receive universal service support.").

past, certain parties have argued that some of those services could be provided only through circuit-switched, TDM technologies. For example, various states require providers to offer local dial tone service, rotary pulse dialing operability, dual-tone multi-frequency signaling, single-party service, SS7 signaling, and single-party revertive calling.[55] Similarly, the federal ETC rules require providers to offer several POTS-like features, such as access to interexchange service and access to operator and directory services, *see* 47 C.F.R. § 54.101(a), as well as functionalities that seem to assume service is provided over TDM, such as dual-tone multi-frequency signaling and single-party service, *see id.* Together, therefore, COLR and other legacy service obligations could, conceivably, preclude carriers in some areas from retiring their legacy POTS technologies. To be sure, it may be possible to satisfy regulatory service obligations with equivalent IP technology in some cases, but these archaic rules were clearly designed for different markets in a different era. The ambiguity regarding the scope of these rules itself can serve as an impediment to investing in IP infrastructure.

These service obligations made sense (if they ever did) only in the era of local exchange monopolies, when the Commission's goal was ensuring that every consumer had access to POTS service. Today, however, these legacy obligations no longer serve their intended purpose, but instead *undermine* federal universal service policy with respect to broadband and IP-enabled services.

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[55] *See, e.g.*, Ohio Rev. Code Ann. § 4927.01(A)(1) (defining "'[b]asic local exchange service'" to include local dial tone service); Wis. Admin. Code PSC § 160.03(2)(a)(3) (requiring rotary pulse dialing); Kan. Stat. Ann. § 66-1187(p), (q) (requiring tone dialing and SS7 signaling); Mo. Code Regs. Ann. tit. 4, § 240-32.100(2)(B) (requiring dual tone multi-frequency signaling); Mo. Code Regs. Ann. tit. 4, § 240-32.100(2)(E) (requiring "SS7 . . . or an enhanced version thereof, down to the tandem level of the switching hierarchy"); Wis. Admin. Code PSC § 160.03(2)(a)(7) (requiring "[s]ingle party revertive calling, if 2 or more pieces of customer premises equipment can be simultaneously active on the line or channel being used by the customer").

First, in some cases these obligations may make it difficult (or even impossible) for carriers to retire the PSTN, thereby requiring certain providers to maintain legacy TDM and IP facilities when both are not required — a costly and inefficient outcome that diverts capital from broadband deployment. As discussed, some service obligations are defined by reference to a particular network architecture or presume a carrier uses TDM technology. Maintaining both circuit-switched *and* packet-switched facilities is expensive — and each dollar that a carrier is forced to invest in the former may be one fewer dollar that can be invested in deployment of next-generation broadband facilities and services. By one estimate, ILECs spent approximately $25 billion on capital expenditures in 2008, and over fifty percent of that amount (52.2 percent) was spent on their legacy facilities.[56] In other words, much of the capital resources of some of the largest communications providers in the country is directed not towards deployment of next-generation IP infrastructure, but rather towards maintaining legacy facilities.

Second, service obligations that compel just one carrier — the ILEC — to offer service to substantially all customers in a designated service territory, frequently without any federal or state high-cost universal service support, effectively impose an unfunded mandate and are inconsistent with a procurement-model approach to universal service. If the Commission concludes, as it should, that the time has come to abolish command-and-control, public-utility-style regulation and adopt a new regulatory compact that relies on consent rather than compulsion, it will need to replace legacy service obligations with a new regulatory paradigm. Regulators should promote universal service in high-cost areas not by unilaterally imposing a duty to serve, but instead through explicit agreements with providers that agree to serve a

[56] *See* Robert C. Atkinson & Ivy E. Schultz, *Broadband in America: Where It Is and Where It Is Going* at 29-30 (Columbia Inst. for Tele-Info. Nov. 11, 2009), *available at* http://www.broadband.gov/docs/Broadband_in_America.pdf.

specific area for a specific period of time in return for a specific amount of universal service funding. Federal ETC obligations and state COLR obligations are fundamentally at odds with this efficient, technologically neutral approach to ensuring universal service.

In sum, legacy service obligations, where they apply, are inconsistent with federal universal service policy and frustrate the Commission's goal of ensuring that *all* Americans have access to broadband and IP-enabled services. Many state policymakers are likely to recognize this and conclude that they, too, have a compelling interest in eliminating outdated service obligations that impede broadband deployment in their states. However, if the states do not take steps to fundamentally reform these obligations consistent with the new federal regime, the Commission should intervene and replace them with an approach to universal service that better advances the Commission's broadband goals. For the reasons discussed in the remainder of this section, the Commission has authority to take such steps to advance federal universal service policy.

B. The Commission Has Authority To Reform Legacy ETC Obligations and Adopt Uniform Service Obligations for Recipients of Broadband Funding

The Framework calls for elimination of legacy ETC obligations at the same time the Commission eliminates its legacy, POTS-focused universal service programs. In the meantime, the Framework calls for immediately scaling back those legacy service obligations. In some areas today, the federal service obligation applies regardless of whether carriers actually receive any federal high cost support. As a first step, when adopting the Framework the Commission should make clear going forward that legacy ETC obligations only apply to carriers in areas where they actually receive federal high cost support. Moreover, though functionally equivalent IP services may suffice, it is the case today that legacy ETC obligations are based on traditional circuit-switched telecommunications technology. *See, e.g.*, 47 C.F.R. § 54.101(a) (discussing "voice grade access to the public switched network," "local usage," "dual tone multi-frequency signaling," and "single-party service."). Those requirements, too, should be eliminated immediately.

Finally, the Framework calls for a more flexible approach to eligibility determinations for broadband funding, under which the Commission would have exclusive jurisdiction to designate eligible broadband providers and establish their service obligations. Adopting these reforms is well within the Commission's power.

1. The Commission Can Eliminate Legacy ETC Service Obligations When It Ceases To Provide Universal Service Support for Circuit-Switched Telecommunications Services

The Commission has clear authority to free telecommunications carriers of their legacy ETC obligations when it eliminates its existing high-cost universal service programs. The statutory provision that imposes those obligations is section 214(e)(1), which provides that ETCs "shall, throughout the service area for which the [ETC] designation is received . . . offer *the services that are supported by Federal universal service support mechanisms* under section 254(c)[.]" 47 U.S.C. § 214(e)(1) (emphasis added). Today, ETC obligations require carriers to offer circuit-switched or equivalent telecommunications services throughout their designated service areas. But once those services are no longer "supported by Federal universal service support mechanisms," then, under the plain language of section 214(e), service providers will have no continuing obligation under that provision to offer them.

2. The Commission Has Authority To Eliminate Legacy ETC Obligations Immediately in Those Areas Where a Carrier Is Not Receiving Universal Service Support

The Commission also has authority to immediately scale back legacy ETC obligations to prevent them from impeding broadband deployment. As it transitions high-cost universal service funding from the existing mechanisms to the new broadband mechanism, the Commission can immediately modify these outdated legacy ETC obligations in two ways.

First, the Commission can reinterpret section 214(e)(1) so that an ETC has an obligation to serve a given geographic area *only* when the ETC actually receives high-cost support for that area.[57] The Commission has previously interpreted this provision as requiring an ETC to provide supported services *throughout its service area*, regardless of whether the ETC is receiving any high-cost support in that area.[58] But this is not the only permissible interpretation of the statutory language. The Commission can reinterpret it to mean that a carrier's obligation to offer service applies only in those geographic areas where the carrier is receiving support — *i.e.*, where the services "are supported."[59] Under this interpretation, even if an ILEC technically is an ETC for a large "service area," its actual service obligations would be far less expansive.

Second, the Commission can direct the states to redefine the "service areas" of existing ETCs so that they include only those locations where the ETCs are receiving legacy support. Section 214(e)(5) states that an ETC's " 'service area' means a geographic area established by a State commission . . . for the purpose of determining universal service obligations and support mechanisms." 47 U.S.C. § 214(e)(5). While this subsection establishes a presumption that the

[57] Again, that provision states that ETCs "shall, throughout the service area for which the designation is received . . . offer the services *that are supported by* Federal universal service support mechanisms under section 254(c) . . . ." 47 U.S.C. § 214(e)(1) (emphasis added).

[58] *See* Section III.A, *supra.*

[59] By contrast, where the ETC *is* receiving high-cost support, it would be required to provide the services and functionalities set forth in 47 C.F.R. § 54.101(a). Similarly, where a carrier is receiving E-rate or Rural Health Care funding, it would be required to provide the services supported by those programs to eligible customers in a manner consistent with the Commission's rules.

"service area" for a so-called "rural" carrier is its "study area,"[60] Congress established no such presumption for a "*non*-rural" carrier's service area — and thus plainly envisioned that it would be *smaller* than its study area. *See id.* Consistent with this notion, the Commission in its *First Universal Service Order* encouraged states to define small service areas when designating non-rural carriers as ETCs. *See First Universal Service Order* ¶ 116. But, despite the urging of the Commission (and the Joint Board),[61] many states have designated non-rural carriers as ETCs for their entire study areas.

At the time, the Commission warned that this action might be unlawful because it would interfere with federal universal service goals.[62] Specifically, the Commission noted that, "if a state commission adopts as a service area for its state the existing study area of a large ILEC, this action would erect significant barriers to entry" for competitive providers, undermining universal service and potentially violating section 254(f).[63] Here, too, excessively large service-area designations hinder federal policy — in this case, the deployment of broadband services. Accordingly, the Commission can deem those designations "inconsistent with the Commission's rules to preserve and advance universal service,"[64] and direct the states to redefine ETC service

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[60] 47 U.S.C. § 214(e)(5) ("In the case of an area served by a rural telephone company, 'service area' means such company's 'study area' unless and until the Commission and the States, after taking into account recommendations of a Federal-State Joint Board . . . establish a different definition of service area for such company."). Importantly, the Communications Act defines "rural" telephone companies largely in terms of their size, not their customers; larger "non-rural" companies actually serve the bulk of the nation's rural and other high-cost lines. *See* 47 U.S.C. § 153(37) (defining "rural telephone company").

[61] *See* Recommended Decision, *Federal-State Joint Board on Universal Service*, 12 FCC Rcd 87, ¶¶ 176-177 (1996) ("*Joint Board Recommended Decision*").

[62] *See First Universal Service Order* ¶¶ 184-185.

[63] *Id. See also Joint Board Recommended Decision* ¶¶ 176-177 (noting that excessively large ETC service areas "could potentially violate section 254(f)" by undermining the Commission's efforts to preserve and advance universal service).

[64] 47 U.S.C. § 254(f).

areas to encompass only those places where ETCs receive legacy high-cost universal service support.

Section 214 does give the states discretion over various aspects of the ETC designation process. But the Commission has authority to interpret the text of section 214, and to the extent that the statutory language is ambiguous, the courts must defer.[65] That deference should be especially generous in this context, because section 254 of the 1996 Act grants the Commission broad authority to implement the entire federal universal service program, of which ETC designations form only a small part. The Commission recognized as much in the *Western Wireless Order*, noting that state commissions do not "have unlimited discretion" under 214(e) to adopt policies that thwart federal universal service goals, and that to conclude otherwise would "effectively undermine[] congressional intent in adopting the universal service provisions of section 254."[66]

In any event, the Commission has authority to preempt the states' ETC-designation decisions under the theories discussed below in Section III.C.2 insofar as they negate federal policy goals. ETC obligations can have the same effect on broadband deployment as state legacy service obligations, and when imposed in the absence of explicit universal service funding, they

[65] With respect to section 214 in particular, the Tenth Circuit has noted that "[t]he FCC's interpretation of the Telecommunications Act's provisions addressing state ETC designations is, of course, subject to deference." *WWC Holding Co. v. Sopkin*, 488 F.3d 1262, 1273 (10th Cir. 2007).

[66] Declaratory Ruling, *Western Wireless Corporation Petition for Preemption*, 15 FCC Rcd 15168, ¶ 29 (2000) ("*Western Wireless Order*") ("While Congress has given the state commissions the primary responsibility under section 214(e) to designate carriers as ETCs for universal service support, we do not believe that Congress intended for the state commissions to have unlimited discretion in formulating eligibility requirements . . . . [W]e do not believe that Congress intended to grant to the states the authority to adopt eligibility requirements that have the effect of prohibiting the provision of service in high-cost areas by non-incumbent carriers. To do so effectively undermines congressional intent in adopting the universal service provisions of section 254.") (footnote omitted).

can constitute an unfunded mandate and are inconsistent with the procurement-model approach to universal service. Thus, the justifications discussed below for preempting legacy state service requirements also apply to states' ETC designation decisions.

3. *The Commission Has Exclusive Jurisdiction To Designate Providers Eligible for Broadband Funding*

The Commission also has authority to exercise exclusive jurisdiction in designating which providers should be eligible for support from the new broadband funding mechanisms. Nothing in the statute requires that broadband eligibility determinations be performed under the cumbersome process outlined in section 214(e), which provides for a state role. Rather, section 214(e)(2) grants state commissions authority only to "designate a *common carrier* . . . as an eligible *telecommunications* carrier." 47 U.S.C. § 214(e)(2) (emphases added). Because broadband Internet access is an information service subject to exclusive FCC jurisdiction,[67] the Commission has authority to create a separate process for evaluating which providers of that service should be eligible for broadband funding.[68]

State commissions nonetheless might assert a right to attach conditions to a provider's receipt of federal broadband support. The Commission can make clear that it will preempt such conditions. Importantly, section 2(b) does not constrain the Commission's power to preempt

[67] *See, e.g.*, Declaratory Ruling, *Inquiry Concerning High-Speed Access to the Internet over Cable and Other Facilities*, 17 FCC Rcd 4798, ¶¶ 38-40 (2002), *aff'd in part, vacated in part*, *Brand X Internet Servs. v. FCC*, 345 F.3d 1120 (9th Cir. 2003), *rev'd*, *NCTA v. Brand X Internet Servs.*, 545 U.S. 967 (2005); Report and Order, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14853, ¶¶ 1-3 (2005); Declaratory Ruling, *Appropriate Regulatory Treatment for Broadband Access to the Internet over Wireless Networks*, 22 FCC Rcd 5901, ¶ 2 (2007); *see also* Report to Congress, *Federal-State Joint Board on Universal Service*, 13 FCC Rcd 11830, ¶¶ 76-80 (1998).

[68] As the Commission has recognized, many rural LECs offer broadband transmission as a telecommunications service. *2011 NPRM* ¶ 60 n.68. Thus, if the Commission relies solely on section 254 in establishing its broadband universal service funding mechanisms, states may have a role in designating these "broadband ETCs" under section 214.

state rules concerning eligibility for broadband funding. That provision limits the Commission's jurisdiction only with respect to "*intrastate* communication service[s],"[69] and broadband Internet access is a jurisdictionally interstate service. Thus, under a traditional preemption analysis, the Commission may preempt state conditions on broadband funding to the extent that they " 'stand[] as an obstacle to the accomplishment and execution of the full purposes and objectives' " of federal universal service policy concerning broadband deployment. *Concepcion*, 131 S. Ct. at 1753 (citation omitted). Moreover, as an independent ground for preemption, the Commission may rely on section 254(f), which bars states from adopting any regulations that are "inconsistent with the Commission's rules to preserve and advance universal service" or that "burden" federal universal service mechanisms. 47 U.S.C. § 254(f). Here, not only would additional state eligibility requirements be "inconsistent" with a federal policy not to impose such requirements, they also would "burden" federal mechanisms by deterring providers from participating in the broadband funding program and increasing the bids of the few providers willing to be subjected to those state requirements.

C. The Commission Has Authority To Ensure That State Commissions Fundamentally Transform or Eliminate Obsolete COLR and Legacy Service Obligations

As discussed above, state COLR obligations thwart the Commission's broadband goals in essentially the same ways as federal ETC mandates. Recognizing this, many states have acknowledged that their obsolete service requirements must change in order to facilitate the transition to next-generation communications networks. Some states have eliminated their COLR and other legacy service obligations altogether,[70] and others have dramatically scaled

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[69] 47 U.S.C. § 152(b)(1) (emphasis added).

[70] Florida, for example, eliminated all COLR requirements effective January 1, 2009. Likewise, for companies electing to provide retail services on a deregulated basis, South

them back.[71] Many more are actively considering eliminating their existing obligations. The Commission should encourage states to transform their legacy obligations so that they promote, rather than impede, broadband deployment. However, if states fail to achieve such reforms by the time the Commission eliminates legacy ETC obligations, the Commission can preempt any remaining COLR and legacy service obligations as inconsistent with federal universal service policy.[72]

1. State Adoption of a Procurement-Model Approach to Universal Service

The Framework proposes the following approach in order for states to retain COLR and other service obligations consistent with the Commission's universal service goals (including not

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Carolina has eliminated COLR obligations except with respect to a small number of grandfathered, stand-alone residential basic POTS customers.

[71] Louisiana has eliminated COLR obligations for certain telephone exchanges based on the existence of competition, and has established a procedure by which carriers may obtain relief from COLR obligations in additional exchanges based on a showing of competition. Missouri recently enacted legislation that, among other things, allows telecommunications companies to elect not to be a COLR in certain counties, thereby relieving such companies of requirements to provide or offer basic local or basic interexchange service. *See* H.R. 339, 96th Leg., 1st Sess. (Mo. 2011) (amending RSMo § 392.460(3)), *available at* http://www.house.mo.gov/billtracking/bills111/billpdf/truly/HB0339T.PDF (enacted June 22, 2011). North Carolina recently enacted legislation that relieved of their COLR obligations those LECs that are subject to alternative regulation. *See* S.R. 343, 2001-52 Sess. (N.C. 2011), *available at* http://www.ncleg.net/Sessions/2011/Bills/Senate/PDF/S343v4.pdf. Texas has enacted legislation specifying that deregulated companies and transitioning companies are not required to fulfill the obligations of a provider of last resort ("POLR"). S.R. 980, 82d Leg., Reg. Sess. (Tex. 2011), *available at* http://www.capitol.state.tx.us/tlodocs/82R/billtext/pdf/SB00980F.pdf#navpanes=0. And Wisconsin enacted legislation that allows ILECs to obtain waivers of their POLR obligation to make basic voice service available to all residential customers and that sunsets altogether the statute imposing POLR obligations after April 30, 2013. *See* S.R. 13, Spec. Sess., 2011 Wis. Act 22, § 117 (Wisc. 2011), *available at* http://legis.wisconsin.gov/ 2011/data/acts/11Act22.pdf (adding Wis. Stats. § 196.503).

[72] The Commission proposed to do just that in the draft order attached as Appendix C to its November 5, 2008 Further Notice of Proposed Rulemaking. *See 2008 NPRM*, Appx. C. Specifically, the Commission's order would have required winning bidders in the auction for broadband funding to assume "all of the [COLR] obligations of the incumbent LEC for [the ILEC's] study area, whether such obligations are imposed on the LEC pursuant to state or federal law." *Id.* ¶ 39.

burdening the federal universal service support mechanisms). First, states would need to provide explicit universal service support that fully compensates carriers for the costs of complying with state-imposed service obligations. This could be accomplished only through an explicit funding mechanism and not through implicit support, such as that embedded in retail rates or intercarrier compensation. Second, states could no longer impose COLR or other service obligations on any carrier without its consent. Instead, states should enter into an express agreement with a COLR, under which that carrier would agree to serve a specific geographic area for a specific period of time in exchange for a specific amount of state universal service support. States could not unilaterally abrogate the terms of the agreement or force a carrier to bear additional obligations without its consent.

If the states were to make these reforms, their service obligations likely would not conflict with federal universal service policy. Indeed, were states to provide explicit support to offset the costs of maintaining legacy services, such funding could support dual-use facilities that also support broadband offerings. Similarly, if states were to adopt a new approach to universal service that relies on consent rather than compulsion, such a regime would avoid unfunded mandates and be consistent with the Commission's procurement-model approach to universal service.

2. Preemption of State Legacy Service Obligations

Although some states will reform their legacy service obligations, others will not. Where states do not modify those obligations, consistent with the approach described above, the Commission can preempt those obligations as inconsistent with federal universal service policy. The Commission can base such preemption authority on a number of independent, mutually reinforcing, grounds.

Traditional preemption analysis. The Commission has authority to preempt state legacy service obligations on the ground that they impermissibly regulate jurisdictionally mixed facilities in a manner that negates federal universal service policy.

The Commission has recognized that "requiring an incumbent to maintain two networks — one copper and one fiber — would be costly [and] possibly inefficient, and reduce the incentive for incumbents to deploy fiber facilities." *National Broadband Plan* at 49. The Commission can now adopt a clear federal policy that encourages upgrading networks with next-generation, IP equipment and facilities. If the Commission does so, it would have a strong basis for preempting state service obligations. As numerous courts have held, the legacy POTS architecture is jurisdictionally mixed because it carries both interstate and intrastate communications.[73] Further, to the extent they preclude carriers from retiring their existing facilities, state service obligations are fundamentally inconsistent with a federal policy that IP networks can replace legacy facilities when the latter are no longer capable of providing the advanced services that consumers want and need. It is hornbook law that where it is *physically impossible* to implement both federal policy (retirement of legacy facilities) and state policy (continued provision of legacy facilities) with respect to facilities used indivisibly for interstate and intrastate services, federal policy must prevail despite section 2(b) of the Communications Act.[74]

[73] *See, e.g., PSC of Md.*, 909 F.2d at 1515 ("[W]e have frequently held that services provided locally by the LECs which support access to the interstate communications network have interstate as well as intrastate aspects.").

[74] *See Louisiana PSC*, 476 U.S. at 375-76 n.4; *see also NARUC III*, 880 F.2d at 429 (where state regulation would "negate[] the exercise by the FCC of its own lawful authority over interstate communication[s]" "state authority must yield to national imperatives"); *California*, 39 F.3d at 933 (concluding that preemption was clearly appropriate where "compliance with conflicting state and federal . . . rules would in effect be impossible").

Along similar lines, the Commission can conclude that state legacy service obligations negate the Commission's policy of ensuring that broadband is deployed throughout the nation. Granted, unlike with retirement of POTS facilities, it may not be *physically* impossible to achieve the goal of universal broadband deployment in the face of state COLR and other legacy service obligations. But, as discussed above, such obligations do make it *economically infeasible* for some carriers to roll out broadband service in high-cost areas. That is sufficient to justify federal preemption, despite section 2(b).[75]

For example, in *California v. FCC*, the Ninth Circuit upheld the Commission's preemption of state regulations requiring structural separation of the facilities and personnel used by BOCs to provide jurisdictionally mixed enhanced services. *See* 39 F.3d at 931-33. The FCC acknowledged that compliance with both state and federal requirements was technically possible. *See id.* at 933. But because "it would not be *economically feasible* for the BOCs to offer the interstate portion of such services on an integrated basis while maintaining separate facilities and personnel for the intrastate portion," the state regulation would necessarily result in structural separation of *both* interstate and intrastate services, thus impeding the Commission's policy of abolishing such restrictions. *Id.* at 932-33 (emphasis added).[76] Accordingly, preemption was appropriate.

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[75] *See, e.g.*, *PSC of Md.*, 909 F.2d at 1515 (preemption is appropriate where "(1) the matter to be regulated has both interstate and intrastate aspects[;] . . . (2) FCC preemption is necessary to protect a valid federal regulatory objective[;] . . . and (3) state regulation would 'negate the exercise by the FCC of its own lawful authority' because regulation of the interstate aspects of the matter cannot be 'unbundled' from regulation of intrastate aspects.") (citations omitted).

[76] *See also California*, 39 F.3d at 922 ("*[B]ecause of economic and operational factors*, enhanced service providers would separate their facilities for services that are offered both interstate and intrastate, thereby *essentially negating the FCC's goal* of allowing integrated provision of enhanced and basic services.") (emphases added).

Similarly, in the *NCUC* cases, the Fourth Circuit upheld the Commission's preemption of state regulations prohibiting subscribers from connecting their own equipment to the telephone network unless that equipment was used *exclusively* for interstate service.[77] Even though it was physically possible for the state and federal regulations to coexist — because subscribers could use provider-supplied equipment for intrastate calls and their own equipment for interstate calls[78] — the court concluded that preemption was permissible. It noted that "[u]sually it is not feasible, as a matter of economics and practicality of operation, to limit the use of such equipment to either interstate or intrastate transmissions," and thus the "practical effect" of the state regulation would be to prohibit attachment of customer-provided equipment for *all* calls.[79] And because this would negate the federal policy permitting attachment of customer-provided equipment to the interstate network, the Commission had authority to preempt the contrary state regulation. *See NCUC I*, 527 F.2d at 793; *NCUC II*, 552 F.2d at 1043.

Here, too, it is impossible to limit the detrimental effect of state service obligations to the intrastate jurisdiction alone; rather, such regulations have the "practical effect" of making it infeasible to deploy jurisdictionally interstate broadband facilities in many high-cost areas. Thus, the Commission can preempt them as inconsistent with federal universal service goals. Indeed, this was the very conclusion reached by the Commission in the *Western Wireless Order*.

[77] *See NCUC I*, 537 F.2d 787; *NCUC II*, 552 F.2d 1036. The Supreme Court cited both of these cases with approval in *Louisiana PSC. See* 476 U.S. at 375-76 n.4.

[78] *See NCUC I*, 537 F.2d at 791; *NCUC II*, 552 F.2d at 1043; *see also California*, 39 F.3d at 933 ("The Fourth Circuit acknowledged that it was possible to comply with both the states' and the FCC's regulations: customers could have one telephone for interstate use and one for intrastate use.").

[79] *NCUC I*, 537 F.2d at 791, 793; *see also NCUC II*, 552 F.2d at 1043 (noting the "practical and economic impossibility" of providing separate equipment for the interstate and intrastate jurisdictions); *California*, 39 F.3d at 933 ("[I]t was highly unlikely, due to practical and economic considerations, that customers would maintain two separate phones.").

There, the Commission preempted state regulations that amounted to an unfunded COLR obligation for competitive ETCs,[80] noting that, "[t]o the extent that a state's [ETC requirements] . . . also involve[] matters properly within the state's intrastate jurisdiction under section 2(b) of the Act, such matters that are inseparable from the federal interest in promoting universal service in section 254 remain subject to federal preemption." *Western Wireless Order* ¶ 27 (footnote omitted).

Finally, if the Commission were to adopt a procurement-model approach to universal service, it could preempt any remaining state COLR and other service obligations on the basis that they directly negate that federal policy, including by imposing unfunded mandates. As discussed above, legacy service obligations that *compel* incumbent providers to offer service are inconsistent with a new regulatory paradigm under which providers incur service obligations only to the extent that they consent to them in explicit agreements with regulators.[81] Given this, the Ninth Circuit's decision in *California* is directly on point. As with elimination of structural separation requirements, the Commission cannot achieve its deregulatory goals by eliminating legacy service obligations on the federal level alone. *See* 39 F.3d at 931-33. Rather, state command-and-control policies *must* be eliminated for the Commission to transition from the existing public-utility-style regime to a new procurement-model approach. Accordingly, the Commission could readily demonstrate that "its regulatory goals . . . would be negated" if it does not preempt state service obligations. *Id.* at 933.

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[80] The state regulation in question required competitive telecommunications carriers to provide service throughout an ILEC's service area before being designated as an ETC in that service area. *See Western Wireless Order* ¶¶ 30-31.

[81] For this reason, the Commission can preempt service obligations even in those states that allow providers to satisfy their obligations using IP technology. Absent the consent of the provider in exchange for explicit funding, these obligations are unfunded mandates and inconsistent with the procurement-model approach to universal service.

Section 254(f). The Commission also has authority to preempt any remaining state service obligations because they contravene section 254(f) of the 1996 Act. Section 254(f) provides that state universal service rules are permissible only if: (i) they are "not inconsistent with the Commission's rules to preserve and advance universal service," (ii) they "do not rely on or burden Federal universal service support mechanisms," *and* (iii) they require "[e]very telecommunications carrier that provides intrastate telecommunications services [to] contribute, on an equitable and nondiscriminatory basis . . . to the preservation and advancement of universal service in that State." 47 U.S.C. § 254(f).

State service obligations satisfy none of these requirements. *First*, as discussed above, those legacy burdens are "inconsistent with" the Commission's efforts to achieve ubiquitous deployment of broadband services. *Id.* They constitute unfunded mandates and are inconsistent with the procurement-model approach to universal service. *Second*, those obligations "burden Federal universal service support mechanisms." In some cases, they may require carriers to offer POTS service in areas where it is uneconomic to do so, thereby increasing those carriers' need for legacy universal service support. They also are likely to increase the demand for support from the broadband universal service fund, because POTS-oriented service obligations force providers to spend capital on legacy services instead of investing that capital in broadband deployment. *See id.*[82] *Third*, because most states impose service obligations only on ILECs, those obligations are not an "equitable and nondiscriminatory" form of promoting universal service. *Id.* Given this, the Commission would be well within its authority under section 254(f) to preempt state service obligations in the event that states do not eliminate those obligations

[82] *See also WWC Holding*, 488 F.3d at 1277 ("Section 254(f) authorizes a state to create its own universal service standards *only to the extent that a state is providing state funding to meet those standards*. To hold otherwise would ignore the last and longest sentence of Section 254(f).") (emphasis added).

themselves.[83] And because the statute itself supplies the source of the Commission's preemption power, section 2(b) of the Communications Act poses no obstacle to the Commission's assertion of jurisdiction.[84]

As the Tenth Circuit has explained, "[f]or regulation aimed at promoting universal service, Section 254(f) provides a hierarchy in which states cannot conflict with the federal universal services program[.]" *WWC Holding*, 488 F.3d at 1272. And the Commission has repeatedly interpreted the statute as foreclosing state requirements that undermine federal universal service goals, explaining earlier this year that "section 254(f) . . . bars states from adopting regulations that are inconsistent with the rules established by the Commission to preserve and advance universal service."[85] In the *Western Wireless Order,* the Commission relied on section 254(f) in preempting a state requirement that a competitive carrier "provide service throughout [an ILEC's] service area prior to designation as an ETC" there. *Western Wireless Order* ¶ 31. The Commission noted that such a requirement — which is essentially an unfunded COLR obligation for competitive carriers — "discourages 'emerging technologies' from entering high-cost areas" and, accordingly, would be "inconsistent with the Commission's universal service policies and rules" in violation of section 254(f). *Id.*; *see also id.* ¶ 27. As discussed above, state legacy service obligations have the same effect on ILECs, often forcing

[83] Even if the statute were ambiguous, a reviewing court would be required to defer to the Commission's interpretation of section 254(f). *See, e.g., Qwest Communications Int'l, Inc. v. FCC*, 398 F.3d 1222, 1229-30, 1233 (10th Cir. 2005).

[84] The Supreme Court held in *Iowa Utilities Board* that, after the 1996 Act, the states retain jurisdiction over intrastate matters only "[i]nsofar as Congress has remained silent." 525 U.S. at 381 n.8. Here, because section 254(f) expressly precludes states from adopting universal service rules that are "inconsistent with" federal regulation, the Commission has authority to preempt even regulations that apply only to intrastate communications.

[85] Notice of Proposed Rulemaking, *Lifeline and Link Up Reform and Modernization*, 26 FCC Rcd 2770, ¶ 258 & n.458 (2011).

them to incur unfunded obligations and deterring them from deploying broadband capability in high-cost areas.

CONCLUSION

The Commission has ample legal authority to adopt the joint proposals set forth in the Framework.